PO-CH/NL/0499 PT B

PO CH/NL/0499
PART. B.

PO CH/NL/0499
PART. B.

1989 BUDGET
FINANCIAL SECTOR
BORROWING REQUIREMENTS.

1.3.89

CLOSED

THIS FOLDER HAS BEEN
REGISTERED ON THE
REGISTRY SYSTEM

mp.pc/Riley/079

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

BUDGET

COPY NO. 1 OF 32 COPIES

FROM: C J RILEY
DATE: 23 February 1989

CHANCELLOR

* Thanks. Prefer ② as variant; and amend other passim.

SECRET

cc Chief Secretary
Financial Secretary
Paymaster General
Economic Secretary
Sir P Middleton
Sir T Burns
Mr Anson
Mr Wicks
Mr Scholar
Mr Culpin
Mrs Lomax
Mr Sedgwick
Mrs Butler
Mr S Davies
Mr Gilhooly
Mr Mowl
Mr Macpherson
Miss Simpson
Miss Wallace
Mrs Chaplin
Mr Tyrie
Mr Call

Sir Anthony Battishill)
Mr Beighton)
Mr Isaac) IR
Mr Painter)
Mr Calder)

Mr Unwin)
Mr Jefferson-Smith) C&E

B.L.O.

FSBR CHAPTER 1

I attach a draft of Chapter 1. The text follows the style used last year. Various different versions of table 1.1 are included, showing alternative ways in which the NICs change and the abolition of the earnings rule might be presented. Table 1.2 is essentially the version submitted yesterday by Colin Mowl.

SECRET

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

BUDGET SECRET
BUDGET LIST ONLY
NOT TO BE COPIED

BUDGET SECRET
BUDGET LIST ONLY
NOT TO BE COPIED

2. You will wish to consider the order of the measures in table 1.1, and the degree of aggregation. If the NIC package is included with the tax measures, you will want to consider whether it comes at the beginning or the end. You may also want to consider whether to put the excise duties (and VAT) nearer the end, after the savings measures, as in Chapter 4 and in last year's FSBR; but when they were frozen in 1987 they were placed near the beginning because of the relatively large numbers involved.

3. You will also wish to consider which measures should be mentioned in paragraph 1.05, and in what order. The present draft relates to a non-indexed base, mentioning the indexing of allowances but not the freezing of excise duties. Working from an indexed basis would mean mentioning the duties but not the allowances.

4. Four versions of table 1.1 are given, as follows:-

Variant 1

This includes the NIC package immediately after the tax measures, but before striking the total. The gross public expenditure cost of abolishing the earnings limit is placed immediately below the total, with a footnote indicating that it will be met entirely from the Reserve. It would clearly not be right to include the gross expenditure effects in the total cost of the package.

Variant 2

This includes abolition of the earnings limit before striking the total. A row of dots is given for it in the table, but a footnote indicates that there will be gross public expenditure effects, met from the Reserve. Note that a line of zeros in the table would not indicate the true net cost of this measure, since it would ignore tax flowbacks.

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

Variant 3

In this variant, both the NIC package and the earnings limit are included under the title "other measures" after the total cost of the tax measures has been struck. Because the cost of abolishing the earnings limit is scored gross, it is not possible to add this to the cost of the NIC package to yield a grand total for the cost of the package.

Variant 4

This is the same as variant 3, except that a row of dots is given for abolishing the earnings limit, as in variant 2. The total cost of the budget measures is given in the final row of the table.

5. These variants are all consistent with inclusion of abolition of the earnings limit in Chapter 4, along with the NIC package. FP propose to include a description of the change, including a reference to gross public expenditure costs and tax flowbacks, at the end of the main text of Chapter 4, but no entry in table 4.1. The paragraph on "budget consequentials" in chapter 5 would presumably need to include a reference to the gross expenditure cost in any event, noting that this will be charged to the Reserve and not add to planning totals.

6. All the figures in table 1.1 are consistent with the figures in today's Scorecard. Those in table 1.2 take on board your preliminary comment on the version submitted yesterday.

ie net 14·0/12·0

CJR

C J RILEY

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

<chapter> 1 The Budget

1.01. The objective of the Government's economic policy is to defeat inflation and to maintain a vigorous and enterprising economy, with sustained growth of output and increased employment.

1.02. The Financial Statement and Budget Report (FSBR) supplements the Chancellor's Budget Statement. It presents the Medium Term Financial Strategy (MTFS); describes developments in the economy over the past year; provides forecasts to mid-1990; sets out the tax proposals in the Budget; summarises the Government's spending plans; and gives forecasts for the public finances for the year ahead.

<side> **The Medium Term Financial Strategy**

1.03. Chapter 2 describes the MTFS, which provides the framework for the Government's economic policy. The objectives of the MTFS and the central role of monetary policy have remained unchanged throughout the 1980s, a period of substantial economic progress. Monetary policy is designed to ~~bring down~~ reduce the growth of money GDP over the medium term, so bringing down inflation. It is

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

buttressed by a sound fiscal policy, with a substantial Budget surplus in both 1988-89 and 1989-90.

~~conducted within a sound fiscal framework;~~ in this year's MTFS a gradual return to ~~budget~~ a balanced Budget is projected over the medium term, with both taxes and public expenditure declining as a share of GDP. The MTFS is complemented by policies designed to improve the working of markets and the supply performance of the economy.

<side> **The economy**

economic trends

1.04. Chapter 3 describes the main developments in the economy in 1988 and the prospect until mid-1990. In recent years ~~developments~~ have ~~been~~ become increasingly difficult to interpret because of inconsistencies within the national and sectoral accounts; adjusted figures that reduce (but do not eliminate) these inconsistencies are used throughout the FSBR. The economy grew strongly again in 1988, with the largest fall in unemployment since the war. GDP is forecast to grow by a further 2½ per cent in 1989, ~~though~~ on the basis of growth through the year, ~~is forecast to be lower.~~ Inflation ~~should~~ be on a downward trend ~~again~~ in the second half of 1989.

is forecast to

approximately

lower than this.

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

<side> **Tax and National Insurance measures**

I'd re-order as marked

1.05. Chapter 4 sets out the tax and National Insurance proposals in the Budget. They include indexation of the main income tax allowances, abolition of stamp duty on shares, improvements to personal equity plans and employee share schemes, reform of the taxation of life assurance, pensions, and unit trusts, measures to promote unleaded petrol, ~~simplification and deregulation of VAT; and~~ reform and reduction of employee National Insurance contributions, together with abolition of the earnings rule for pensioners. The measures are summarised in table 1.1.

<side> **Public expenditure**

1.06. Chapter 5 summarises the Government's spending plans, as set out in the public expenditure White Paper. This chapter also provides the latest estimate of the outturn for the public expenditure planning total in 1988-89.

<side> **Public sector finances**

1.07. Chapter 6 presents the complete financial picture for the public sector. The public sector debt repayment is forecast to be [£14 billion] in 1988-89. A further debt repayment of [£12 billion] is forecast for 1989-90, equivalent to £7 billion net of privatisation proceeds, the same as in 1988-89. The forecast takes account of the measures in the Budget which are expected to reduce taxation and National Insurance contributions by £1.9 billion, after adjusting for the net cost of indexing direct and indirect tax rates and allowances. Table 1.2 shows the main components of general government receipts and expenditures.

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

VARIANT 1

TABLE 1.1 THE BUDGET MEASURES[1]

£ million			yield (+)/cost (-)
	1989-90		1990-91
	Changes from a non-indexed base	Changes from an indexed base	Changes from an indexed base
Income Tax			
personal allowances and basic rate limit indexed	-1465	-	-
car benefit scales increased	+ 90	+ 90	+ 110
Schedule E put on receipts basis	- 60	- 60	- 80
Excise duties			
petrol, derv etc	-	- 545	- 580
duty on unleaded petrol reduced, surcharge added to 2 star petrol	- 30	- 30	- 75
vehicle excise duty	+ 40	- 150	- 170
tobacco	-	- 235	- 250
alcohol	-	- 255	- 280
Value Added Tax			
non- domestic construction etc	+ 315	+ 315	+ 540
bad debt relief, reform of registration rules etc	- 105	- 105	- 270
Stamp duty on shares abolished	+ 10	+ 10	- 900
Life assurance businesses' tax regime reformed	- 20	- 20	+ 45
Reforms to pensions, personal equity plans, employee share schemes and unit trusts	- 5	- 5	- 10
Corporation Tax			
small companies' rate threshold increased	*	*	- 35
Other tax changes	- 70	- 35	+ 25
National Insurance Contributions	- 860	- 860	-2440
Total	-2160	-1885	-4370
Pensioners' earnings limit abolished[2]	- 125	- 125	- 250

1 These measures, and the basis of the costings shown, are described in detail in chapter 4.

2 Cost shown is gross public expenditure, which will be met from the Reserve. See Chapter 5.

fp.nh/sf/42

VARIANT 2

TABLE 1.1 THE BUDGET MEASURES[1]

I may well drop this measure

£ million	1989-90		1990-91
yield (+)/cost (-)	Changes from a non-indexed base	Changes from an indexed base	Changes from an indexed base
Income Tax			
personal allowances and basic rate limit indexed	-1465	-	-
car benefit scales increased	+ 90	+ 90	+ 110
Schedule E put on receipts basis	- 60	- 60	- 80
Excise duties			
petrol, derv etc	-	- 545	- 580
duty on unleaded petrol reduced, surcharge added to 2 star petrol	- 30	- 30	- 75
vehicle excise duty	+ 40	- 150	- 170
tobacco	-	- 235	- 250
alcohol	-	- 255	- 280
Value Added Tax			
non- domestic construction etc	+ 315	+ 315	+ 540
bad debt relief, reform of registration rules etc	- 105	- 105	- 270
Stamp duty on shares abolished	+ 10	+ 10	- 900
Life assurance businesses' tax regime reformed	- 20	- 20	+ 45
~~Reforms to pensions, personal equity plans, share schemes and unit trusts~~	~~- 5~~	~~- 5~~	~~- 10~~
Corporation Tax			
small companies' rate threshold increased	*	*	- 35
Other tax changes	- ~~70~~ 75	- ~~35~~ 40	+ ~~25~~ 15
National Insurance Contributions	- 860	- 860	-2400
Pensioners' earnings limit abolished[2]	..	..	..
Total	**-2160**	**-1885**	**-4370**

1 These measures, and the basis of the costings shown, are described in detail in chapter 4.

2 Public expenditure cost of £250m will be met from the Reserve. See Chapter 5.

Why is CGT set-off for unincorporated companies included in 'other tax changes'?

fp.nh/sf/43

VARIANT 3

TABLE 1.1 THE BUDGET MEASURES[1]

£ million			yield (+)/cost (-)
	1989-90		1990-91
	Changes from a non-indexed base	Changes from an indexed base	Changes from an indexed base
Tax Measures			
Income Tax			
personal allowances and basic rate limit indexed	-1465	-	-
car benefit scales increased	+ 90	+ 90	+ 110
Schedule E put on receipts basis	- 60	- 60	- 80
Excise duties			
petrol, derv etc	-	- 545	- 580
duty on unleaded petrol reduced, surcharge added to 2 star petrol	- 30	- 30	- 75
vehicle excise duty	+ 40	- 150	- 170
tobacco	-	- 235	- 250
alcohol	-	- 255	- 280
Value Added Tax			
non- domestic construction etc	+ 315	+ 315	+ 540
bad debt relief, reform of registration rules etc	- 105	- 105	- 270
Stamp duty on shares abolished	+ 10	+ 10	- 900
Life assurance businesses' tax regime reformed	- 20	- 20	+ 45
Reforms to pensions, personal equity plans, share schemes and unit trusts	- 5	- 5	- 10
Corporation Tax			
small companies' rate threshold increased	*	*	- 35
Other tax changes	- 70	- 35	+ 25
Total	**-1300**	**-1025**	**-1930**
Other measures			
National Insurance contributions reformed	- 860	- 860	-2440
Pensioners' earnings limit abolished[2]	- 125	- 125	- 250

1 These measures, and the basis of the costings shown, are described in detail in chapter 4.

2 Cost shown is gross public expenditure, which will be met from the Reserve. See Chapter 5.

BUDGET SECRET
BUDGET LIST ONLY
NOT TO BE COPIED

fp.nh/sf/44

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

VARIANT 4

TABLE 1.1 THE BUDGET MEASURES[1]

£ million	1989-90 Changes from a non-indexed base	1989-90 Changes from an indexed base	yield (+)/cost (-) 1990-91 Changes from an indexed base
Tax Measures			
Income Tax			
personal allowances and basic rate limit indexed	-1465	-	-
car benefit scales increased	+ 90	+ 90	+ 110
Schedule E put on receipts basis	- 60	- 60	- 80
Excise duties			
petrol, derv etc	-	- 545	- 580
duty on unleaded petrol reduced, surcharge added to 2 star petrol	- 30	- 30	- 75
vehicle excise duty	+ 40	- 150	- 170
tobacco	-	- 235	- 250
alcohol	-	- 255	- 280
Value Added Tax			
non- domestic construction etc	+ 315	+ 315	+ 540
bad debt relief, reform of registration rules etc	- 105	- 105	- 270
Stamp duty on shares abolished	+ 10	+ 10	- 900
Life assurance businesses' tax regime reformed	- 20	- 20	+ 45
Reforms to pensions, personal equity plans, share schemes and unit trusts	- 5	- 5	- 10
Corporation Tax			
small companies' rate threshold increased	*	*	- 35
Other tax changes	- 70	- 35	+ 25
Total tax measures	-1300	-1025	-1930
Other measures			
National Insurance contributions reformed	- 860	- 860	-2440
Pensioners' earnings limit abolished[2]	..	..	..
Total Budget measures	-2160	-1885	-4370

1 These measures, and the basis of the costings shown, are described in detail in chapter 4.

2 Public expenditure cost at £250m will be met from the Reserve. See Chapter 5.

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

BUDGET SECRET
BUDGET LIST ONLY
NOT TO BE COPIED

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

Table 1.2 The finances of the Public Sector[1]

£ billion	1988-89: 1988 Budget[2]	1988-89: Latest estimate	1989-90: Forecast
RECEIPTS			
Inland Revenue:			
Income tax	42.1	43.5	47.1
Corporation tax[3]	19.8	18.8	22.0
Petroleum revenue tax	1.2	1.3	1.3
Capital gains tax	2.0	2.4	2.1
Inheritance tax	1.0	1.1	1.1
Stamp duties	2.0	2.3	2.6
Total Inland Revenue	**68.0**	**69.4**	**76.1**
Customs and Excise:			
Value added tax	26.2	27.5	29.8
Petrol, derv duties etc	8.4	8.7	8.7
Tobacco duties	5.0	5.1	5.1
Alcohol duties	4.5	4.6	4.7
Betting and gaming duties	0.9	0.9	0.9
Car tax	1.3	1.4	1.4
Customs duties	1.6	1.7	1.8
Agricultural levies	0.1	0.2	0.1
Total Customs and Excise	**47.9**	**49.9**	**52.5**
Vehicle excise duties	2.8	2.8	2.9
Oil royalties	0.6	0.6	0.6
Gas levy	0.4	0.4	0.4
Local authority rates[4]	19.0	18.9	20.4
Other taxes and royalties	2.5	2.7	2.8
Total taxes and royalties	**141.2**	**144.8**	**155.7**
National insurance and other contributions	31.6	32.8	34.6
Interest and dividends	5.6	6.6	6.7
Gross trading surpluses and rent	3.5	3.3	3.5
Other receipts	2.9	3.3	3.4
General Government Receipts	**184.9**	**190.8**	**203.8**

£ billion	1988-89: 1988 Budget[2]	1988-89: Latest estimate	1989-90: Forecast
EXPENDITURE			
Social security	48.5	47.4	51.0
Health	20.7	21.8	23.2
Defence	19.2	19.0	20.1
Education and science	18.0	18.4	19.6
Home office and legal departments	7.0	7.2	8.0
Transport	5.1	4.8	5.4
Scotland	8.5	8.7	9.0
Wales	3.5	3.6	3.8
Northern Ireland	5.1	5.6	5.5
Other departments	22.8	21.7	23.1
Privatisation proceeds	-5.0	-7.0	-5.0
Reserve	3.5	-	3.5
Public expenditure planning total	**156.9**	**151.1**	**167.1**
General government gross debt interest	17.5	18.2	16.6
Other adjustments	8.6	9.2	9.5
General Government Expenditure	**183.0**	**178.5**	**193.2**

Receipts, expenditure and debt repayment

£ billion	1988-89: 1988 Budget[2]	1988-89: Latest estimate	1989-90: Forecast
General government receipts	184.9	190.8	203.8
General government expenditure	183.0	178.5	193.2
General government debt repayment	2.0	12.3	10.6
Public corporations' market and overseas debt repayment	1.2	1.7	1.5
Public sector debt repayment	**3.2**	**14.0**	**12.1**

1 In this and other tables constituent items may not add up to totals because of rounding.
2 On current definitions.
3 Includes advance corporation tax (net of repayments): 5.3 6.0 6.4
- also includes North Sea corporation tax after ACT set off and corporation tax on gains.
4 In this and other tables community charge receipts are included with local authority rates.

I have already commented on earlier version

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

BUDGET SECRET

BUDGET SECRET

B.L.O. SECRET

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

COPY 1 of 19 COPIES

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

BUDGET

FROM: N I MACPHERSON

DATE: 23 FEBRUARY 1989

1. MR GILHOOLY

2. CHANCELLOR

cc Financial Secretary
Economic Secretary
Sir P Middleton
Sir T Burns
Mr Scholar
Mr Culpin
Mr Riley
Mr A C S Allan
Mr Matthews
Mrs Chaplin
Mr Tyrie

Sir A Battishill IR
Mr Calder IR

Mr Unwin C & E
Mr P R H Allen

a
A few comments marked

AA

SECRET

FSBR CHAPTER 4

Attached is a redraft of Chapter 4.

2. The NIC and earnings rule changes have been included under a national insurance heading. Earnings rule abolition does not appear in table 4.1 since it is primarily a public expenditure measure. Its cost is therefore reported in the narrative section.

B.L.O.

3. Regarding the questions you asked on the first draft:

(i) Close companies pay corporation tax rather than income tax. We have therefore assumed up to now that the special higher rate would also be corporation tax. Mr Reid of the Revenue is going to send you a minute on this.

sent to you last night

(ii) There are five classes of VED for buses and coaches. Including all the rates in the narrative section may give this change more emphasis than you want.

(iii) Taxis have always been central to the proposed changes to hackney VED classes. This is because it has

SECRET

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

seemed inequitable that taxis which spend a great deal of time on the road should pay less VED than the family car.

(iv) The pension proposals are revenue neutral in the short and medium term. They have a positive yield in the very long run - 20 years or so out. The reference to the long term effect in the annex has been dropped.

4. The Economic Secretary has yet to see the redraft of the ECJ judgement section provided by Customs and Excise.

Nick Macpherson

N I MACPHERSON

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

4 The Budget Tax and National Insurance Proposals in Detail

4.01 The main tax and national insurance changes proposed in the Budget are summarised below. A full list of changes is given in Table 4.1.

Income tax

4.02 The main income tax thresholds will be increased in line with the statutory indexation provisions (based on the increase of 6.8 per cent in the RPI in the year to December 1988); the higher level of age allowance currently for those aged 80 and over will be extended to those aged 75 and over. This will mean that:

the single person's and wife's earned income allowances will rise from £2,605 to £2,785;

the married allowance will rise from £4,095 to £4,375;

the additional personal allowance and widow's bereavement allowance will rise from £1,490 to £1,590;

the age allowance for those aged 65 to 74 will rise from £3,180 to £3,400 (single) and from £5,035 to £5,385 (married);

the age allowance for those aged 75 and over will rise from £3,150 for those under 80 and from £3,310 for

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

those aged 80 and over to £3,540 (single), and from £5,035 for those under 80 and from £5,205 for those aged 80 and over to £5,565 (married);

the income limit for age allowance will rise from £10,600 to £11,400;

the basic rate limit will rise from £19,300 to £20,700 of taxable income.

4.03 The age allowance withdrawal rate will be reduced from £2 of allowances for each £3 of income to £1 for each £2 of income above the limit of £11,400.

Benefits in kind

4.04 Car benefit scale charges will be increased by 20 per cent from 6 April 1989.

Private medical insurance

4.05 Income tax relief will be given from April 1990 on private medical insurance premiums for those aged 60 and over.

Charitable giving

4.06 The limit on charitable donations qualifying for tax relief under the payroll giving scheme will be doubled from £240 to £480 a year from 6 April 1989.

Employee share ownership plans (ESOPs)

4.07 Tax relief will be given for payments by companies to qualifying ESOP trusts.

Approved employee share schemes

4.08 The annual limit for individual participation in 1978 employee share scheme will be increased to £2,000 or - if greater - 10 per cent of pay up to a maximum of £6,000. The 1980 SAYE share scheme limit will be increased from £100 to £150 per month. The maximum discount from the share price at which options may be

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

granted under these schemes will be doubled to 20 per cent.

Profit-related pay

4.09 The cash ceiling on the amount of profit-related pay attracting tax relief will be increased to £4,000. A number of other changes will simplify and improve PRP.

Personal equity plans

4.10 The annual limit on investment in Personal Equity Plans will be increased from £3,000 to £4,800. The annual limit on investment in unit and investment trusts will be increased to £2,400, irrespective of other holdings and restricted to unit and investment trusts which invest mainly in UK equities. The PEP rules will be greatly simplified.

Schedule E assessment

4.11 The basis of assessment for Schedule E (remuneration of employees and directors) will be changed from earnings to receipts. In practice, most employees are taxed on this basis already.

Relocation expenses

4.12 Payments an employer makes towards the additional housing costs of an employee transferred to a more expensive location will no longer be exempt from tax.

Pensions

4.13 The tax regime for pensions will be amended. For occupational schemes the main features will be:

employers will be able to set up "top up" schemes for their employees, with no limits on benefits, but without special tax reliefs;

a limit will be placed on pensions paid from tax approved schemes, based on earnings of £60,000 a year. This is consistent with a privileged pension of up to £40,000 a year or maximum tax free lump sum of up to £90,000. The ~~earnings~~ limit will be indexed to prices;

the rules for tax approved pensions, particularly affecting those who take early retirement, will be simplified and improved.

These changes will apply to schemes set up on or after Budget day and to new members joining existing schemes on or after that date.

4.14 New simplified rules will be introduced for monitoring additional voluntary contributions. Any surplus contributions made will be returned to employees, subject to a special tax charge.

4.15 Annual contribution limits for personal pension schemes will be increased as a percentage of earnings, subject to an overall cash limit based on the £60,000 earnings limit for occupational schemes.

Life assurance

The tax regime for life assurance companies will be ~~[illegible]~~ reformed. The main changes,

4.16 ~~The following are the main changes for life assurance companies~~ to be introduced from 1 January 1990:

pension and general annuity business expenses will be deductible only from pension or general annuity profits;

BUDGET SECRET
BUDGET LIST ONLY
NOT TO BE COPIED

relief for expenses of acquiring new life assurance business (other than pension or general annuity business) will be spread over seven years: this change will be phased in gradually over the next four years;

the rate of tax charged on income and capital gains attributable to policy holders will be reduced to a rate equal to the basic rate of income tax (25 per cent);

life assurance policy duty will be abolished.

Stamp Duties

4.17 Stamp duties on share transactions will be abolished from 1 April 1990.

Unit trusts

4.18 A new tax regime will be introduced from 1 January 1990 for unit trusts investing in transferable securities which are freely marketable throughout the European Community under the UCITS directive. The rate of corporation tax charged on their income will be reduced to a rate equal to the basic rate of income tax (25 per cent).

COBO and deep discounted bonds

4.19 The new issues queue will be abolished by a general consent under the Control of Borrowing Order and the regime for deep discount bonds, including certain index-linked bonds, will be amended with effect from Budget day.

Business taxation

4.20 The profits limit for the small companies' corporation tax rate of 25 per cent for financial year 1989 will be raised

from £100,000 to £150,000 and the limit for marginal relief will be raised from £500,000 to £750,000.

4.21 The main rate of corporation tax for the financial year 1989 will be 35 per cent.

4.22 The apportionment rules for close companies will be abolished. Special provisions including a corporation tax rate equal ~~linked~~ to the higher rate of income tax (40 per cent) will be introduced for close investment companies which distribute less than a specified percentage of their profits.

X

4.23 Unincorporated business~~men~~es ~~who~~ which make trading losses which can be set off against their other income will be able to set off any unused balance of their losses against capital gains.

X

Capital gains tax

4.24 The capital gains tax annual exempt amount will remain at £5,000 in the case of individuals and £2,500 in the case of most trusts.

4.25 Capital gains tax deferral on lifetime gifts will be restricted to certain types of gift - in particular, gifts of business and heritage assets, gifts on which there is an immediate charge to inheritance tax, and gifts to charity.

? Add increase in chattels exemption from £3000 ⇒ £5000

yes

Inheritance tax

4.26 From Budget day the threshold for inheritance tax will be increased in line with the statutory indexation provisions from £110,000 to £118,000.

VAT

4.27 The present turnover requirements for VAT registration will be replaced for most businesses by a single limit based on turnover in the previous twelve months.

4.28 From 15 March 1989 the VAT registration limit will ~~become~~ be raised to £23,600 a year.

4.29 Changes will be introduced to make relief from VAT on bad debts more widely available.

4.30 The default surcharge regime will be eased by reducing the maximum rate of penalty from 30 per cent to 20 per cent.

4.31 As announced on 6 February, to comply with the European Court judgement of 21 June 1988, a new VAT regime will apply to non-residential construction and property development. Landlords will be given the option to tax rent from non-residential buildings. VAT at the standard rate will be applied to

[EST to lookout]

- news services (but not newspapers);
- protective boots and helmets supplied to employers;
- fuel and power supplied to businesses; and
- water and sewerage services supplied to industry.

cp: [Still nothing on transition]

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

4.33 VAT relief for charities will be extended to charity fund-raising events, certain types of advertising and medical sterilising equipment. Cars leased to the disabled will be relieved of car tax.

Excise duty

Should this be "just under 1p a litre" (just over 3p a gallon) etc?

Yes

4.34 The duty on unleaded petrol will be reduced by the equivalent of just over 3p a gallon (nearly 1p a litre) including VAT. A higher rate of duty will be introduced on 2 and 3 star petrol. This will add 5p a gallon (just over 1p a litre) including VAT to the tax charged on these grades.

ITV levy

4.35 From 1 January 1990, the additional payments made by ITV programme contractors will be assessed on a mixture of net advertising revenue and profits.

Tax administration

4.36 In the light of recommendations by the Keith Committee, changes will be made:

This all sounds v threatening.

Ask FST to redraft

- to update the system of monetary penalties for tax offences;
- to modernise the powers of the Inland Revenue to obtain information;
- to improve compliance by employers.

Tax confidentiality

4.37 Criminal sanctions will be provided against unlawful disclosure of information relating to ~~an identifiable~~ a taxpayer by employees or former employees of the ~~revenue departments.~~ Inland Revenue or Customs and Excise.

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

National Insurance

4.38 From [1] October, changes are proposed to the structure of national insurance. ~~Unless otherwise stated, the decisions announced on [y] November 1988 will apply.~~

4.39 The £70 and £105 a week earnings limits for Class 1 national insurance contributions are due to rise to £75 and £115 from April 1989. From [1] October 1989, for employees only the £75 limit will become a threshold and the 7 per cent band between £75 and £115 will be abolished. Employees earning over £75 a week will therefore pay Class 1 contributions at a rate of 5 per cent on their first £75 and 9 per cent on earnings above £75 up to the upper earnings limit. The structure of Class 1 employee contributions for those earning under £75 a week will remain unchanged.

This is option 4 — likely to need amending to 2%/9%.

Yes — Sount [illegible]

Contribution payable will be 2 per cent of earnings below the lower earnings limit plus 9 per cent of earnings above the lower earnings limit, up to the upper earnings limit. Those earning below the lower earnings limit will continue to pay no national insurance contributions.

4.40 The upper earnings limit of £305 a week is due to rise to £325 a week from April 1989. From [x] October, the upper earnings limit will be raised to £355 a week.

Pensioners' Earning Rule

4.41 From x October the rule whereby state retirement pensioners earning more than £75 a week have their pensions reduced, and those earning over £120 a week have their pension abated entirely, will be abolished. ~~It is estimated that~~ The gross public expenditure cost of abolition will be about £125 million in 1989-90 and £250 million in 1990-91. ~~However,~~ This cost will be met from the Reserve, and ~~This measure~~ is

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

therefore not included in Table 4.1. ~~[It is estimated that tax and benefit flowbacks to the exchequer will be £30 million in 1989-90 and £75 million in 1990-91.]~~

(Nor does table 4.1 include the increases in tax and national insurance contribution revenue that will flow from these changes, estimated at £30 million in 1989-90 and £75 million in 1990-91.)

4.42 The~~se~~ changes to National Insurance Contributions and to the pensioners' earnings rule will be included in the Social Security Bill now before Parliament.

NB. I have not included 'benefit flowbacks', tho' these should be included if significant. The NICs bit. I have referred on, of course, employers'?

Table 4.1 Direct effects of changes in taxation and national insurance

See Annex 4 Paragraph numbers		£ million — Estimated effect on receipts in: 1989-90 — Changes from a non-indexed base	1989-90 — Changes from an indexed base	1990-91 — Changes from an indexed base
	INLAND REVENUE			
	Income tax			
1	Increase in single allowance of £180 and married allowance of £280	-1130	-	-
2	Increase in additional personal allowance and widow's bereavement allowance of £100	-10	-	-
3	Increase age allowances in line with statutory indexation	-100	-	-
4	Extend higher age allowances for those aged 80 and over to those aged 75 and over	-10	-10	-15
5	Increase in income limit for age allowance of £800	-15	-	-
6	Increase in basic rate limit of £1,400 to £20,700	-210	-	-
7	Reduction in age allowance withdrawal rate	-5	-5	-5
8	Fringe benefits] car benefit scales 20% increase in	+90	+90	+110
9	Additional housing costs and removal expenses (?) Removal of ESC on [or Fringe Benefits: but are they?]	+5	+5	+30
10	Tax relief for private medical insurance for those aged 60 and over	-	-	-40
11	Pension - amendments to tax rules	*	*	*
12	Payroll giving to charities - increase in donation limit to £480 a year	*	*	*
13	Membership covenants to heritage charities	-5	-5	-10
14	Liberalisation of profit-related pay legislation	-10	-10	-15
15	Increase in approved employee share limits	*	*	*
16	Employee priority in public offer of shares	*	*	*
17	Changes in material interest tests	*	*	-5
18	Abolition of tax relief on new loans to buy Business Expansion Scheme shares	[*	*	+5]
19	Schedule E - change to receipts basis of assessment	-60	-60	-80
20	Changes in settlements provisions where settlor or spouse can benefit	*	*	*
21	Tax deductible from tax credit payments to US companies	-	-	-
	Income tax and corporation tax			
22	Taxation of income, gains and profits of life assurance companies	[*	*	+125]
23	Abolition of close company apportionment	*	*	*
24	Capital allowances - safety at sports grounds and miscellaneous amendments	*	*	*
25	Extension of relief for pre-trading expenditure	*	*	*
26	Subcontractor tax scheme - reduction in voucher requirements	-	-	-
	Income tax and capital gains tax			
27	Personal Equity Plans - increase in limits etc	-5	-5	-10
28	Unincorporated businesses - set off of trading losses against gains	-	-	[-25]

pse check..

* = Negligible   - = Nil

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

Table 4.1 Direct effects of changes in taxation and national insurance

£ million

See Annex 4 Paragraph numbers		Estimated effect on receipts in: 1989-90: Changes from a non-indexed base	1989-90: Changes from an indexed base	1990-91: Changes from an indexed base
	Income tax, corporation tax and capital gains tax			
29	Keith committee - administrative changes	*	*	*
30	Deep discounted bonds - taxation of uplift as income	-	-	+15
31	Tax charge on switching investments in offshore funds	*	*	*
	Corporation tax			
32	Increase in profits limits for small companies rate and marginal relief	*	*	-35
33	Changes in the taxation of certain unit trusts	-	-	*
34	Relief for payments to ESOP trusts	*	*	*
35	Advance corporation tax amendments	*	*	*
36	Sales of subsidiaries	*	*	*
	Capital gains tax			
37	No change in annual exempt amount	-	*	+10
38	Restriction of gifts relief	*	*	+25
39	Change in the rules for Lloyd's underwriters	-	-	*
	Capital gains tax and corporation tax			
40	UK branches of foreign businesses - changes affecting capital gains	*	*	*
41	Technical changes associated with rebasing of capital gains	*	*	*
42	Increase in capital gains chattels exemption to £5000	*	*	*
43	Exemption of certain bonds from charges on capital gains	*	*	*
	Capital gains tax and inheritance tax			
44	Gifts to housing associations	*	*	*
	Inheritance tax			
45	Increase of £8000 in threshold	-35	-	-
46	Changes in rules for varying dispositions on death	+5	+5	+15
	Stamp duties			
47	Abolition of duties on shares	[+50	+50	-850]
48	Abolition of life assurance policy duty	-20	-20	-80
	TOTAL INLAND REVENUE	-1465	+35	-835

* = Negligible   - = Nil

Reduction in tax rate for ✓

[so Chattels exemption applies to companies too?]

Pls check (v. odd)

Table 4.1 Direct effects of changes in taxation and national insurance

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

BUDGET SECRET B.L.O. SECRET

£ million

See Annex 4 Paragraph numbers		Estimated effect on receipts in: 1989-90 Changes from a non-indexed base	1989-90 Changes from an indexed base	1990-91 Changes from an indexed base
	CUSTOMS AND EXCISE			
	Value added tax			
49	Revised registration rules	-35	-35	-100
50	Increase in registration limit	*	*	*
51	Bad debt relief	-50	-50	-150
52	Keith - review of default surcharge	-20	-20	-20
53	Recovery of overpaid VAT and excise duty	-	-	-
54	Revised tax regime for construction, buildings and land	+310	+310	+440
55	Change in liability of news services	+5	+5	+5
56	Change in liability of certain protective boots and helmets	*	*	*
57	Change in liability of certain supplies of fuel and power	-	-	+95
58	Change in liability of certain water and sewerage services	-	-	*
59	Reliefs for charities	-5	-5	-5
60	Relief for research and development cars	-5	-5	-5
61	Car tax Relief for vehicles leased to disabled	-5	-5	-10
	Excise duties			
61	No change in rate of spirits duty	-	-65	-70
62	No change in rate of beer duty	-	-140	-155
63	No change in rate of duty on cider and perry	-	-5	-5
64	No change in rate of duty on wine and made-wine	-	-45	-50
65	No change in rate of duty on 4 star petrol etc	-	-440	-485
66	No change in rate of duty on derv	-	-95	-105
67	No change in rate of duty on minor oils	-	-10	-10
68	No change in rates of tobacco products duties	-	-235	-250
69	Restriction on blending of duty-paid made-wine	*	*	*
70	Determination of original gravity of beer	*	*	*
71	Reduction in duty on unleaded petrol	-30	-30	-60
72	Increase in duty on 2 star and 3 star petrol	*	*	-15
	TOTAL CUSTOMS AND EXCISE	+165	-670	-935
	Vehicle excise duty			
73	No change in VED on cars, light vans and main lorry rates	-	-190	-210
74	Increase in VED rates for taxis, buses and coaches	+20	+20	+20
75	Increase in certain other VED rates	+20	+20	+20
	TOTAL VED	+40	-150	-170
	Other			
76	ITV levy re-basing	-	-	+60
77	Unauthorised disclosure of confidential information	-	-	-
	TOTAL OTHER	-	-	+60
	TOTAL CHANGES IN TAXATION	-1260	-985	-188[illegible]
	National insurance contributions			
78	Turn £75 earnings limit for employees into threshold	-930	-930	-2660
79	Raise upper earnings limit to £355	+70	+30	+[illegible]
	TOTAL CHANGES TO NATIONAL INSURANCE CONTRIBUTIONS	-860	-860	-24[illegible]

amend

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

ANNEX TO CHAPTER 4

Explanatory notes to Table 4.1

Table 4.1 gives the direct effects of changes in taxation. Estimates are rounded to the nearest £5 million. "Negligible" means less than £3 million.

The direct effect of a tax change is the difference between the yield of the tax which would arise on the basis of the rate of tax, allowances, etc prevailing before the Budget (the pre-Budget regime) and the yield after the changes proposed in the Budget (the post-Budget regime). The difference in yield is generally calculated by applying the pre- and post-Budget regimes to the same tax base. This base is the post-Budget base - that is, the levels of income, consumption, profits, etc forecast for future years on the assumption that all the measures proposed in the Budget take effect.

Tax changes may cause changes in taxpayers' behaviour, which in turn can alter the tax base and hence revenue. The direct effects are estimated subject to the constraint that, in general, total incomes and total expenditure are fixed at their post-Budget levels. Thus the estimates in the table do not include income effects - that is, effects arising solely from the impact of changes in taxes on disposable incomes. Nor do they include the effects of changes in the tax base arising from changes in pre-tax incomes, the general level of prices or other macro-economic variables which may result from the proposed tax change. But other behavioural effects are taken into account where it is thought that they will have a significant effect on the yield.

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

For Customs & Excise taxes and duties, all the estimates of yield incorporate the effects of the tax changes on relative prices and associated changes in the pattern of consumers' expenditure. Aggregate income and consumers' expenditure at factor cost are assumed not to change. This is a slight modification of previous practice in which nominal consumers' expenditure at market prices, rather than at factor cost, was held constant. Examples where behavioural effects are taken into account for Inland Revenue taxes include the abolition of stamp duties on share transactions and changes involving the take-up of a new or modified relief.

The post-Budget forecast of each tax given in Table 1.2 takes account of all the effects of the measures announced in the Budget, and not just the direct effects included in table 4.1.

The figures in the first column of Table 4.1 show the direct effect of the Budget proposals on receipts in 1989-90. Budget proposals are compared with a non-indexed base - that is, with the pre-Budget regime of allowances, thresholds and rates of duty at 1988-89 levels.

The figures in the second column show the direct effect of the Budget proposals on receipts in 1989-90, measured against an indexed base. The indexed base for 1989-90 is obtained by increasing 1988-89 allowances, thresholds and rates of duty by 6.8 per cent, the increase in the RPI over the year to December 1988.

The figures in the third column show the direct effect on receipts in 1990-91, also measured against an indexed base. For this comparison, both the Budget proposals and the indexed base for 1989-90 have been further indexed by the forecast movement in the RPI between the fourth quarters of 1988 and 1989 (shown in Table 3.12).

The remainder of this annex provides a commentary on the Budget proposals in Table 4.1; the paragraph numbers refer to

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

BUDGET

SECRET

B.L.O.

SECRET

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

the lines in this table. Additional information is provided for those proposals where the effect on tax liabilities in the first complete year to which the change applies (full year effect) is substantially different from the effect on receipts in either 1989-90 or 1990-91; or where the impact of the proposal is expected to build up over a period of years.

Income Tax

1 to 6 The increases in the main personal allowances and the basic rate limit are in line with the statutory indexation provisions (based on the increase of 6.8 per cent in the RPI in the year to December 1988). The higher age allowance currently given to those aged 80 and over will be extended to those aged 75 years and over. The cost of indexation for those aged between 75 and 79 is included in line 3.

7 The age allowance withdrawal rate will be reduced from £2 of allowances for each £3 of income to £1 for each £2 of income above the limit of £11,400.

8 For 1989-90 the scales for taxing car benefits will be increased by 20 per cent from their 1988-89 levels.

9 The extra-statutory concession which has exempted from tax certain reimbursements by employers of additional housing costs incurred by their employees who have had to move with their jobs to more expensive locations will be withdrawn from 6 April 1989, subject to transitional arrangements.

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

A statutory relief will be introduced to replace the extra-statutory concession which has exempted certain job-related removal expenses from any charge to income tax.

10 Tax relief will be available (with basic rate relief given at source) for eligible premiums paid in 1990-91 and subsequent years for private medical insurance for those aged 60 years and over. The cost for 1990-91 assumes an increase in take-up in the region of 10 per cent as a result of the new relief. Eventual costs will depend, among other things, on the extent to which medical insurance for the over-60s is promoted and taken up.

11 The amendments to the tax rules for pension schemes will mean that:

for tax approved schemes, earnings over £60,000 will be ignored for the purpose of calculating benefits (consistent with a maximum pension of £40,000, or tax-free lump sum of £90,000). Other amendments will be made to the tax rules to improve early retirement benefits, to allow a two-thirds final salary pension on retirement after 20 years' service between ages 50 and 70 and to simplify calculation of tax-free lump sums. These changes apply to new schemes set up on or after 14 March 1989 and to new members joining existing schemes on or after that date;

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

employers will be able to set up top-up schemes with no limits on benefits, but without tax privileges such as tax-free investment build-up;

new rules will allow surplus voluntary contributions to be returned to the member instead of reducing benefits from the employer's scheme. The voluntary scheme will deduct a 35 per cent charge from the refund to recoup the tax advantages enjoyed on contributions and build-up. There will be a further liability on higher rate taxpayers;

changes will be made to the personal pensions tax rules to increase from 1988-89 the age related contribution limits. The increased limit will be subject to the £60,000 earnings cap. And the rules for calculating tax-free lump sums will be simplified.

These measures are expected to have a broadly neutral revenue effects in the early years.

12 The limit on charitable donations qualifying for relief under payroll deduction schemes will be increased from £240 to £480 from April 1989. The cost will depend on take-up.

13 The conditions for relief for charitable covenants will be relaxed so that where a member of a heritage charity is given free entry to view the charity's property, that benefit will not disqualify the covenant payments from relief. The cost will depend on take-up.

14 Amendments to the profit related pay (PRP) legislation will

abolish the "5 per cent test" on a PRP scheme's eligibility for registration;

increase to £4,000 the cash limit on the amount of PRP attracting tax relief;

allow scheme employers to alter, subject to conditions, the rules of PRP schemes which already registered;

enable PRP schemes to be registered for certain employment units using the profits of the whole business rather than of the employment unit itself.

15 The annual limit on the value of shares which may be given to an employee under an approved all-employee profit-sharing share scheme will be increased, with effect from 6 April 1989, from £1,250 (or 10 per cent of pay up to a maximum of £5,000) to £2,000 (or 10 per cent of pay up to £6,000). The limit on monthly savings made by an employee under an approved savings-related share option scheme (ICTA 1988 Section 185) will be increased, from a day to be appointed, from £100 to £150. The maximum discount on the share price at which options may be granted under these schemes will be increased from 10 per cent to 20 per cent. The use of consortium shares in an approved employee share scheme will be extended to any member of a consortium owning 5 per cent or more of the company's ordinary share capital in place of the previous 15 per cent limit.

16 There will be relaxations in the conditions under which income tax relief is given to employees who benefit by virtue of their employment from priority in applying for a public offer of shares.

17 Changes will be made in the material interest tests relating to an employee's eligibility to participate in an approved employee share scheme or a registered profit-related pay scheme, and an individual's entitlement to close company interest relief. Subject to certain conditions, shares held by a trust of which the employee is a beneficiary will be disregarded when reckoning whether he has material interest.

18 Relief for interest on loans to acquire Business Expansion Scheme shares on or after 14 March 1989 will be abolished.

19 From 6 April 1989 Schedule E emoluments will be assessed for the year in which they are received instead of the year for which they are earned. There will be a transitional cost, but from 1992-93 when the transition is complete, there will be an annual yield of about £50 million.

20 A change will be made to the provisions which treat certain settlement income as the settlor's for higher rate tax purposes to ensure that income from outright gifts between husband and wife will be treated under Independent Taxation as the income of the recipient of the gift. For certain other settlements the present rule will be extended

~~to the basic rate producing~~ a small revenue yield.

21 Legislation will be introduced to make clear the amount of UK tax that is deductible from UK tax credits to which non-residents may be entitled under a double taxation convention. This measure will prevent a potential Exchequer loss of about £15 million a year.

Income tax and corporation tax

22 From 1 January 1990, the rules for taxing life assurance companies will be changed:

to allow relief for the expenses of pension, general annuity and other life assurance business only against their respective profits;

to spread the relief for the costs of acquiring new business (other than pension and general annuity business) over seven years, subject to transitional arrangements in the first four years to phase out the present immediate relief; and

to reduce the corporation tax rate on income and capital gains allowable to policyholders to 25 per cent.

The yield in 1990-91 and the immediately following years is reduced by the proposed transitional arrangements, and by the carry-forward of unrelieved expenses from past years. ~~The yield is likely to peak in 1995-96, diminishing thereafter.~~ The yield in all

far too precise

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

years depends on developments in the industry, particularly in the level of new business, and is therefore highly uncertain.

Shd we rather give 'matching' [illegible] (before the 'declaration')

equal

23 The apportionment rules for close companies will be abolished. A higher rate of corporation tax ~~linked~~ to the higher rate of income tax of 40 per cent will be introduced for close investment companies which distribute less than a specified percentage of their profits. A close investment company will no longer get tax relief for interest payments, annual payments or management expenses unless these would have been deductible if paid by an individual.

24 The legislation relating to capital allowances for safety expenditure at sports grounds will be amended from 1 January 1989 to take account of the extension of safety certificate requirements to regulated stands at undesignated sports grounds. Minor amendments will be made to the capital allowances legislation to correct defects and anomalies in advance of the consolidation of that legislation.

25 The period for which relief may be available for business expenditure incurred before a trade begins will be increased from three to five years. The cost of this proposal will take some years to build up and could amount of tens of millions of pounds.

26 Subject to consultation, the requirements of the scheme for subcontractors in the construction industry will be reduced, for

BUDGET SECRET
BUDGET LIST ONLY
NOT TO BE COPIED

example by aggregation of small payments onto a single voucher.

Income tax and capital gains tax

27 The main changes are:

an increase in the overall annual limit on investment in a Personal Equity Plan to £4,800;

within that an increase in the limit for investment in authorised unit trusts and investment trusts to £2,400, coupled with a new requirement that the trust must invest mostly in UK equities;

significant simplifications for plan managers; and

the facility for new share issues to be brought within plans.

The costs assume take-up in the region of 400,000 in the first full year. The cost is likely to reach £30 million after 5 years.

28 After 5 April 1989, if an unincorporated trader makes a loss which can be set off against other income of the same and/or the following year, he will be able to set any unused loss against his capital gains. The estimated full year costs accrued in 1989-90 and 1990-91 are £50 million and £75 million respectively.

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

Income tax, corporation tax and capital gains tax

29 In the light of recommendations of the Keith Committee, administrative changes will be made:

to update the system of monetary penalties for tax offences in line with inflation and remove obsolete penalties;

to introduce a uniform time limit of 20 years for recovery of tax lost through default;

to allow taxpayers further time to claim reliefs where an Inspector discovers that further tax is due;

to modernise the Inland Revenue's powers to obtain information about a taxpayer under enquiry, to allow questions to be put to the taxpayer, provide greater safeguards for the taxpayer and protect audit papers and tax advice from disclosure by his accountant;

to amend the Inland Revenue's search powers to provide greater safeguards for the taxpayer;

to create a new criminal offence for the deliberate destruction of documents called for under the Inland Revenue's information powers;

to change the filing date for returns of PAYE and NIC deductions by employers from 19 April to 19 May, tighten up the penal-

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

ties for late filing gradually over a period of years, leading to the introduction of automatic penalties for all late filing (but not before 1995).

The effect on revenue in subsequent years is expected to be small.

30 From Budget day the existing corporate deep discount legislation in Schedule 4 ICTA 1988 will be widened to include non-variable deep discounted securities issued by non-corporate borrowers. On a sale or redemption the accrued discount will be taxed as income. Any excess or shortfall will be taxed as a capital gain or loss unless the security is exempt from capital gains tax as a qualifying corporate bond. Where deep discounted securities have variable features so that the precise accrued discount at any particular time cannot be determined in advance (including certain index linked bonds), the whole of the uplift between cost price and sale or redemption price will be taxed as income. The eventual yield is ~~very~~ uncertain but is estimated at around £50 million.

31 A tax charge will be imposed on UK investors on gains when they switch holdings within an offshore fund.

Corporation Tax

32 The profits limit for the small companies' corporation tax rate of 25 per cent for financial year 1989 will be raised from £100,000 to £150,000 and the limit for

BUDGET SECRET
BUDGET LIST ONLY
NOT TO BE COPIED

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

marginal relief will be raised from £500,000 to £750,000

33 From 1 January 1990 all unit trusts that are UCITS (Undertakings for Collective Investment in Transferable Securities) under the relevant European Communities legislation will be subject to corporation tax on their income at a rate of 25 per cent, with no relief being given for interest paid by them. The cost will rise to about £20 million from 1991-92 onwards.

34 Payments made by a company to an ESOP trust will be deductible in calculating its corporation tax liability where the trust meets conditions aimed at ensuring the acquisition of shares in the company by its employees.

35 Various minor changes will be made to the advance corporation tax (ACT) rules concerning a company which is part of a group or consortium.

36 Measures will be introduced to counter avoidance of tax on disposals of subsidiaries in ways which could cause a substantial loss of tax.

Capital Gains Tax

37 The capital gains tax annual exempt amount will remain at £5,000 in the case of individuals and £2,500 in the case of most trusts.

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

38 Capital gains tax gifts relief (which allows deferral on gifts) will be restricted to certain types of gift, the main categories being gifts of business and heritage assets and gifts on which there is an immediate charge to inheritance tax. The revenue yield in 1991-92 is estimated at £40 million. The change will not affect gifts to charities or between spouses.

39 The capital gains tax rules and rules about the transfer of securities applying to assets held by Lloyd's underwriters in their premiums trust funds will be amended to facilitate stock lending to market makers.

Capital Gains Tax and Corporation Tax

40 Changes will be made to the rules for the taxation of capital gains of foreign businesses with UK branches or agencies or with operations on the UK continental shelf. The main effect will be to counter possible developments which could lead to a significant loss of tax.

41 Technical changes will be made in relation to the application of the provisions in the Finance Act 1988 for rebasing the taxation of capital gains to 1982 in certain special situations.

~~Assets The limit on the disposal value~~

42 Chattels with a disposal value of less than £3,000 are exempt from charges on capital gains. The limit will be raised to £5,000.

43 Certain sterling bonds will be exempted from capital gains tax and corporation tax on

BUDGET SECRET
BUDGET LIST ONLY
NOT TO BE COPIED

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

gains. The main effect will be to counter use of the indexation allowance in ways which could cause a significant loss of tax.

Capital gains tax and Inheritance Tax

44 Certain gifts to registered housing associations will qualify for capital gains tax deferral and inheritance tax exemption.

Inheritance Tax

45 The estimated full year cost of indexation attributable to taxable estates in 1989-90 is £80 million.

46 The facility for varying the disposition of a deceased person's assets will be limited to those variations making adequate provision for his or her dependants.

Stamp Duty

47 The following stamp duties will be abolished from 1 April 1990:

the ½ per cent ad valorem duty on the transfer of UK registered securities;

stamp duty reserve tax;

the 1½ per cent duties on the conversion of UK shares into depository receipts or their transfer into clearance services;

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

associated charges on bearer shares and unit trusts units; and

certain fixed duties on share transfers.

Announcement of the abolition of these duties is expected to lead to some rise in the value of share transactions. That will mean an increased yield from stamp duty and value added tax in 1989-90 and from some other taxes, eg capital gains tax in later years. The cost figures in Table 4.1 take account of these additional yields.

48 Life assurance policy duty will be abolished from 1 January 1990. The cost in 1990-91 takes account of the consequential change in corporation tax liability

Value Added Tax:

49 The present VAT registration rules will be replaced by a single requirement based on turnover in the previous twelve months. The existing rules based on anticipated turnover will still apply, in modified form, to large businesses and short term events.

50 From 15 March 1989, the registration limit will become £23,600 a year.

51 A comprehensive system of VAT relief on all debts which are more than 18 months old and which have been written off in the trader's accounts will be introduced. Repayment of the relief, or part of it, will be required

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

where the debt is subsequently paid in whole or in part.

52 The maximum rate of default surcharge will be reduced from 30 per cent to 20 per cent for all appropriate VAT returns due on or after 31 March 1989.

53 The right of taxpayers to recover overpaid VAT, excise duty [and car tax] will be confirmed - subject to certain conditions - and procedures established which will enable VAT accounting errors to be corrected.

54 From 1 April 1989, VAT will be applied at the standard rate to the construction and sale of new non-residential buildings. From 1 August 1989, VAT at the standard rate will be applied, in certain circumstances, to building land; and landlords will be able to opt to charge tax on their non-residential property and land transactions. [Tenants whose landlords opt to tax existing leases will pay tax on only half of the rent in the first year. In the case of charities the phasing in period will be five years.] Transitional relief will allow zero rating to continue for certain developments where legal commitments had been entered into before 21 June 1988.

55 From 1 April 1989, VAT will be applied at the standard rate to news services (but not newspapers).

56 From 1 April 1989, VAT will be applied at the standard rate to protective boots and helmets supplied to employers.

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

57 From 1 July 1990, VAT will be applied at the standard rate to fuel and power supplied to businesses.

58 From 1 July 1990, VAT will be applied at the standard rate to water and sewerage services supplied to industry.

59 VAT relief for charities will be extended to charity and certain other fund-raising events, medical sterilising equipment and classified and certain other types of advertising.

60 From 1 May 1989, all cars used by manufacturers for research and development purposes will be relieved of VAT.

Car Tax

61 From Royal Assent, vehicles leased to the disabled will be relieved of car tax.

Excise duties

62-69 There will be no change in the rates of duty on alcoholic drinks, tobacco products and most hydrocarbon oils.

70 The duty arrangements for made-wine will be brought into line with those applicable to wine [of fresh grapes] by prohibiting duty-paid blending.

71 The rules for determining the original gravity of beer for duty purposes will be clarified.

BUDGET SECRET
BUDGET LIST ONLY
NOT TO BE COPIED

72 The duty on unleaded petrol will be reduced by the equivalent of 3.2p a gallon (0.7p a litre) including VAT.

73 A higher rate of duty will be introduced on 2 and 3 star leaded petrol. This will add 5p a gallon (1.1p a litre) including VAT to the tax charged on these grades. Cost of extra take-up of unleaded petrol exceeds yield from 2 star in 1990-91.

Vehicle excise duties

74 There will be no change in the duties on cars, light vans, motor cycles and most lorries.

75 From 15 March 1989, the number of duty rates for taxis, coaches and lorries will be reduced from over sixty to five and rates will be adjusted.

76 From 15 March 1989, the rates of duty on certain rigid lorries will be increased to bring them more into line with rates for articulated vehicles of similar gross weight. The rate of duty for special types capable of carrying very long, wide or heavy loads will be increased to £3,100.

Other

77 From 1 January 1990, the additional payments made by ITV programme contractors will be assessed on a mixture of net advertising revenue and profits.

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

78 Criminal sanctions will be provided against unlawful disclosure of information relating to an identifiable taxpayer by employees or former employees of revenue departments.

National Insurance Contributions

79 From 1 October 1989, the £75 earnings limit for Class 1 employee contributions will be turned into a threshold and the 7 per cent employee band between £75 and £115 will be abolished. 1600

80 From 1 October 1989, the Upper Earnings Limit will be increased from £325 to £355 a week. The yield (£ million) breaks down as follows:

	1989-90	1990-91
Employees	+110	+350
Employers	-40	-120
Total	+70	+230

Negative yield from employers reflects higher contracted out rebate. 1990-91 costing reflects higher corporation tax yield.

rjb/472

CONFIDENTIAL

pup

FROM: MRS R J BUTLER
DATE: 24 February 1989

PS/CHIEF SECRETARY

cc PPS/Chancellor
Mr Anson
Mr Phillips
Mr Riley
Mrs Lomax
Mr Richardson
Miss Simpson
Mr I Taylor
Miss Adamson

FSBR: CHAPTER 5

We discussed the Chief Secretary's manuscript amendments. You agreed to the suggestions I made and I promised to let you see a copy of the version of paragraph 5.06 that is going to the printers.

2. We can, of course, take on further drafting comments (as well as more up-to-date information) at later stages in the process.

RJButler

MRS R J BUTLER

5.06. The major changes in 1988-89 between programme plans in the 1988 White Paper and the estimated outturn are:

<u>central government</u>: increases arising from NHS pay settlements (£0.9 billion), a capital grant of £0.4 billion associated with the sale of Rover to BAe and ~~to~~ finance for the recapitalisation of Shorts Brothers prior to privatisation (£0.4 billion), are offset by reductions in social security expenditure (£1.0 billion) due mainly to the fall in unemployment; lower payments by the Intervention Board for Agricultural Produce (£0.4 billion) and lower expenditure on employment programmes (£0.4 billion);

<u>local authorities</u>: an overspend of £1.2 billion on planned current expenditure and a net underspend of £0.9 billion on capital expenditure, reflecting higher gross spending (£1.2 billion) offset by higher receipts (£2.1 billion);

<u>nationalised industries and other public corporations</u>: an improvement of £0.5 billion mainly reflecting higher profitability of British Steel prior to privatisation (£0.3 billion) and British Rail (£0.3 billion).

est.ld/james/24 Feb/fsbr

BUDGET CONFIDENTIAL

prp (please add to Ch 4 string)

ECONOMIC SECRETARY TO THE TREASURY

FROM: S M A JAMES
DATE: 24 FEBRUARY 1989

PS/CHANCELLOR

cc: PS/Chief Secretary
PS/Financial Secretary
PS/Paymaster General
Sir P Middleton
Sir T Burns
Mr Anson
Mr Scholar
Mr Culpin
Mr Riley
Mr Sedgwick
Mr Gilhooly
Mr Matthews
Mr Macpherson
Miss Wallace
Mrs Chaplin
Mr Tyrie
Mr Call
PS/IR
Mr Unwin, C&E
Mr Jefferson-Smith, C&E
Mr P R M Allen, C&E
Ms French, C&E

FSBR CHAPTER 4: CUSTOMS AND EXCISE TAX CHANGES

Your minute of 21 February asked the Economic Secretary to review the Customs and Excise contribution to the text of Chapter 4. The Economic Secretary has seen the revised Customs contribution incorporated in the attachments to Mr Macpherson's minute of 23 February.

He has the following comments:

(i) <u>4.31</u> to be replaced by the following:

"To comply with the European Court judgment of 21 June 1988 certain previously zero rated goods and services will be subject to VAT at the standard rate.

As announced on 6 February, the regime will aim to minimise the tax and compliance burden.

Non-residential construction and property development will be liable to VAT from 1 April 1989 with transitional relief for prior contractual commitments. Landlords will be given the option to tax rents of non-residential buildings from 1 August 1989.

VAT will also be applied

from 1 April 1989 to:	protective boots and helmets supplied to employers
:	news services
from 1 July 1990 to :	fuel and power supplied to businesses
:	water and sewerage services supplied to industry.

(ii) **4.34**, line 3: delete "nearly" after "gallon"; line 5: insert "leaded" between "3 star" and "petrol".

(iii) **Annex: Explanatory notes to Table 4.1, VAT paragraph 54**: reorder this so that the reference to option to tax comes before that to building land. Clarify "in certain circumstances" (line 5). Retain the square-bracketed sentence ("Tenants whose landlords opt ...").

SMAJ

S M A JAMES
Private Secretary

chex.ps/aa/8 BUDGET - SECRET

BUDGET LIST ONLY

REF NO. ABSA/89/11

COPY NO. 1 OF 19.

(please staple properly, then prop)

MR MACPHERSON

cc PS/Financial Secretary
PS/Economic Secretary
Sir P Middleton
Sir T Burns
Mr Scholar
Mr Culpin
Mr Riley
Mr Gilhooly
Mr Matthews
Mrs Chaplin
Mr Tyrie

Sir A Battishill - IR
Mr Calder - IR

Mr Unwin - C&E
Mr P R H Allen - C&E

FSBR CHAPTER 4

... The Chancellor was grateful for your minute of 23 February. I attach a copy of the pages of the redraft on which he had comments.

ACSA

A C S ALLAN

BUDGET - SECRET

BUDGET LIST ONLY

a limit will be placed on pensions paid from tax approved schemes, based on earnings of £60,000 a year. This is consistent with a privileged pension of up to £40,000 a year or maximum tax free lump sum of up to £90,000. The earnings limit will be indexed to prices;

the rules for tax approved pensions, particularly affecting those who take early retirement, will be simplified and improved.

These changes will apply to schemes set up on or after Budget day and to new members joining existing schemes on or after that date.

4.14 New simplified rules will be introduced for monitoring additional voluntary contributions. Any surplus contributions made will be returned to employees, subject to a special tax charge.

4.15 Annual contribution limits for personal pension schemes will be increased as a percentage of earnings, subject to an overall cash limit based on the £60,000 earnings limit for occupational schemes.

Life assurance

The tax regime for life assurance companies will be reformed. The main changes,

4.16 ~~The following are the main changes for life assurance companies~~ to be introduced from 1 January 1990:

pension and general annuity business expenses will be deductible only from pension or general annuity profits;

from £100,000 to £150,000 and the limit for marginal relief will be raised from £500,000 to £750,000.

4.21 The main rate of corporation tax for the financial year 1989 will be 35 per cent.

4.22 The apportionment rules for close companies will be abolished. Special provisions including a corporation tax rate ~~linked~~ equal to the higher rate of income tax (40 per cent) will be introduced for close investment companies which distribute less than a specified percentage of their profits.

4.23 Unincorporated business~~men who~~ es which make trading losses which can be set off against their other income will be able to set off any unused balance of their losses against capital gains.

Capital gains tax

4.24 The capital gains tax annual exempt amount will remain at £5,000 in the case of individuals and £2,500 in the case of most trusts.

Add increase in chattels exemption

4.25 Capital gains tax deferral on lifetime gifts will be restricted to certain types of gift - in particular, gifts of business and heritage assets, gifts on which there is an immediate charge to inheritance tax, and gifts to charity.

Inheritance tax

4.26 From Budget day the threshold for inheritance tax will be increased in line with the statutory indexation provisions from £110,000 to £118,000.

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

VAT

4.27 The present turnover requirements for VAT registration will be replaced for most businesses by a single limit based on turnover in the previous twelve months.

4.28 From 15 March 1989 the VAT registration limit will ~~become~~ be raised to £23,600 a year.

4.29 Changes will be introduced to make relief from VAT on bad debts more widely available.

4.30 The default surcharge regime will be eased by reducing the maximum rate of penalty from 30 per cent to 20 per cent.

4.31 As announced on 6 February, to comply with the European Court judgement of 21 June 1988, a new VAT regime will apply to non-residential construction and property development. Landlords will be given the option to tax rent from non-residential buildings. VAT at the standard rate will be applied to

EST to look at (must include something on transition)

- news services (but not newspapers);

- protective boots and helmets supplied to employers;

- fuel and power supplied to businesses; and

- water and sewerage services supplied to industry.

4.33 ~~VAT relief~~ for charities will be extended to charity fund-raising events, certain types of advertising and medical sterilising equipment. Cars leased to the disabled will be relieved of car tax.

Excise duty

4.34 The duty on unleaded petrol will be reduced by the equivalent of ~~just over 3p a gallon (nearly 1p a litre)~~ just under 1p a litre (just over 3p a gallon) including VAT. A higher rate of duty will be introduced on 2 and 3 star petrol. This will add 5p a gallon (just over 1p a litre) including VAT to the tax charged on these grades.

ITV levy

4.35 From 1 January 1990, the additional payments made by ITV programme contractors will be assessed on a mixture of net advertising revenue and profits.

Tax administration

4.36 In the light of recommendations by the Keith Committee, changes will be made:

FST to redraft (to explain a little more of what is proposed, and hence sound less threatening)

- to update the system of monetary penalties for tax offences;
- to modernise the powers of the Inland Revenue to obtain information;
- to improve compliance by employers.

Tax confidentiality

4.37 Criminal sanctions will be provided against unlawful disclosure of information relating to ~~an identifiable~~ a taxpayer by employees or former employees of the ~~revenue departments.~~ Inland Revenue or Customs & Excise

National Insurance

4.38 From [1] October, changes are proposed to the structure of national insurance. [~~Unless otherwise stated, the decisions announced on [y] November 1988 will apply.~~]

4.39 The £70 and £105 a week earnings limits for Class 1 national insurance contributions are due to rise to £75 and £115 from April 1989. From [1] October 1989, for employees only, the ~~£75 limit will become a threshold and the 7 per cent band between £75 and £115 will be abolished. Employees earning over £75 a week will therefore pay Class 1 contributions at a rate of 5 per cent on their first £75 and 9 per cent on earnings above £75 up to the upper earnings limit. The structure of Class 1 employee contributions for those earning under £75 a week will remain unchanged.~~

[something on lines:

contribution payments will be 2 per cent of earnings below the lower earnings limit plus 9 per cent of earnings above the lower earnings limit, up to the upper earnings limit. Those earning below the lower earnings limit will continue to pay no national insurance contributions.]

[4.40 The upper earnings limit of £305 a week is due to rise to £325 a week from April 1989. From [x] October, the upper earnings limit will be raised to £355 a week.]

Pensioners' Earnings Rule

4.41 From x October the rule whereby state retirement pensioners earning more than £75 a week have their pensions reduced, and those earning over £120 a week have their pension abated entirely, will be abolished. ~~It is estimated that~~ The gross public expenditure cost of abolition will be about £125 million in 1989-90 and £250 million in 1990-91. ~~However,~~ This cost will be met from the Reserve ~~. This measure~~ and is therefore not included in Table 4.1. ~~[It is estimated that tax and benefit flowbacks to the exchequer will be £30 million in 1989-90 and £75 million in 1990-91.]~~

(nor does table 4.1 include the increased tax and national insurance contribution revenue that will flow from this change, estimated at £30 million in 1989-90 and £75 million in 1990-91).

4.42 ~~These~~ The changes to National Insurance Contributions and to the pensioners' earnings rule will be included in the Social Security Bill now before Parliament.

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

BUDGET

£ million

See Annex 4 Paragraph numbers		Estimated effect on receipts in 1989-90: Changes from a non-indexed base	1989-90: Changes from an indexed base	1990-91: Changes from an indexed base
	INLAND REVENUE			
	Income tax			
1	Increase in single allowance of £130 and married allowance of £260	-1130	-	-
2	Increase in additional personal allowance and widow's bereavement allowance of £130	-10	-	-
3	Increase age allowances in line with statutory indexation	-100	-	-
4	Extend higher age allowances for those aged 80 and over to those aged 75 and over	-10	-10	-15
5	Increase in income limit for age allowance of £500	-15	-	-
6	Increase in basic rate limit of £1,400 to £20,700	-210	-	-
7	Reduction in age allowance withdrawal rate	-5	-5	-5
8	~~Fringe benefits~~ car benefit scales	+90	+90	+110
9	Additional housing costs and removal expenses	+5	+5	+10
10	Tax relief for private medical insurance for those aged 60 and over	[illegible]	[illegible]	-40
11	Pension - amendments to tax rules	*	*	*
12	Payroll giving to charities - increase in donation limit to £480 a year	*	*	*
13	Membership covenants to heritage charities	-5	-5	-10
14	Liberalisation of profit-related pay legislation	-10	-10	-15
15	Increase in approved employee share limits	*	*	*
16	Employee priority in public offer of shares	*	*	*
17	Changes in material interest tests	*	*	-5
18	Abolition of tax relief on new loans to buy Business Expansion Scheme shares	[*	*	+5]
19	Schedule E - change to receipts basis of assessment	[illegible]	-50	-30
20	Changes in settlements provisions where settlor or spouse can benefit	*	*	*
21	Tax deductible from tax credit payments to US companies	-	-	-
	Income tax and corporation tax			
22	Taxation of income, gains and profits of life assurance companies	[*	*	+125]
23	Abolition of close company apportionment	*	*	*
24	Capital allowances - safety at sports grounds and [illegible]	*	*	*
25	Extension of relief for pre-trading expenditure	*	*	*
26	Subcontractor tax scheme - reduction in [illegible] requirements	-	-	-
	Income tax and capital gains tax			
27	Personal Equity Plans - increase [illegible]	-5	[illegible]	[illegible]
28	[illegible]	[illegible]	[illegible]	[illegible]]

[20] per cent increase in

either: Removal of ESC on
or: Fringe Benefits:
[are they?]

* = Negligible - = Nil

SECRET

B.L.O.

SECRET

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

BUDGET SECRET - BUDGET LIST ONLY

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

[illegible] direct effects of changes in taxation and national insurance

£ million

See Annex + Paragraph numbers		Estimated effect on receipts in: 1989-90 Changes from a non-indexed base	1989-90 Changes from an indexed base	1990-91 Changes from an indexed base
	Income tax, corporation tax and capital gains tax			
29	Keith committee - administrative changes	*	*	*
30	Deep discounted bonds - taxation of uplift as income	-	-	+15
31	Tax charge on switching investments in offshore funds	*	*	*
	Corporation tax			
32	Increase in profits limits for small companies rate and marginal relief	*	*	-35
33	~~Changes in the taxation~~ Reduction in tax rate for of certain unit trusts	-	-	*
34	Relief for payments to ESOP trusts	*	*	*
35	Advance corporation tax amendments	*	*	*
36	Sales of subsidiaries	*	*	*
	Capital gains tax			
37	No change in annual exempt amount		*	+10
38	Restriction of gifts relief	*	*	+25
39	Change in the rules for Lloyd's underwriters	-	-	*
	Capital gains tax and corporation tax			
40	UK branches of foreign businesses - changes affecting capital gains	*	*	*
41	Technical changes associated with rebasing of capital gains	*	*	*
42	Increase in capital gains chattels exemption to £5000	*	*	*
43	Exemption of certain bonds from charges on capital gains	*	*	*
	Capital gains tax and inheritance tax			
44	Gifts to housing associations	*	*	*
	Inheritance tax			
45	Increase of £[illegible] in threshold	[illegible]	[illegible]	[illegible]
46	Changes in rules for varying dispositions on death	[illegible]	*	+[illegible]
	Stamp duties			
47	Abolition of [illegible]	+[illegible]	+[illegible]	+[illegible]
48	Abolition of [illegible]	[illegible]	[illegible]	[illegible]
	Total Inland Revenue	[illegible]	+[illegible]	

* = Negligible - = Nil

Does fact this comes under heading CGT & CT imply chattels exemption applies to companies too?

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

[illegible] direct effects of changes in taxation and national insurance

Budget [illegible]	Estimated effect on receipts in: 1989-90 Changes from a non-indexed base	1989-90 Changes from an indexed base	1990-91 Changes from an indexed base
CUSTOMS AND EXCISE			
Value added tax			
49 Revised registration rules	-35	-35	-100
50 Increase in registration limit	*	*	*
51 Bad debt relief	-50	-50	-150
52 Keith - review of default surcharge	-20	-20	-20
53 Recovery of overpaid VAT and excise duty	-	-	-
54 Revised tax regime for construction, buildings and land	+310	+310	+440
55 Change in liability of news services	+5	+5	+5
56 Change in liability of certain protective boots and helmets	*	*	*
57 Change in liability of certain supplies of fuel and power	-	-	+95
58 Change in liability of certain water and sewerage services	-	-	*
59 Reliefs for charities	-5	-5	-5
60 Relief for research and development cars	-5	-5	-5
CAR TAX 61 Relief for vehicles leased to disabled	-5	-5	-10
Excise duties			
61 No change in rate of spirits duty	-	-65	-70
62 No change in rate of beer duty	-	-140	-155
63 No change in rate of duty on cider and perry	-	-5	-5
64 No change in rate of duty on wine and made-wine	-	-45	-50
65 No change in rate of duty on 4 star petrol etc	-	-440	-465
66 No change in rate of duty on derv	-	-95	-105
67 No change in rate of duty on minor oils	-	-10	-10
68 No change in rates of tobacco products duties	-	-235	-250
69 Restriction on blending of duty-paid made-wine	*	*	*
70 Determination of original gravity of beer	*	*	*
71 Reduction in duty on unleaded petrol	[illegible]	[illegible]	[illegible]
72 Increase in duty on 2 star and 3 star petrol	*	[illegible]	-15
TOTAL CUSTOMS AND EXCISE	+165	[illegible]70	[illegible]35
Vehicle excise duty			
73 No change in VED on cars, light vans and rain lorry rates	-	-	[illegible]
74 Increase in VED rates for taxis, buses and coaches	+[illegible]	+	+[illegible]
75 Increase in certain other VED rates	+[illegible]	+	+[illegible]
TOTAL VED	+[illegible]	[illegible]	[illegible]
Other			
[illegible] re-basing			+[illegible]
Unauthorised disclosure of confidential information			
TOTAL OTHER		-	+[illegible]
TOTAL CHANGES IN TAXATION	[illegible]160	[illegible]5	[illegible]8
National insurance contributions			
[illegible] Turn £75 earnings limit for employees into threshold	[illegible]	[illegible]	[illegible]
[illegible] Raise upper earnings limit to £[illegible]	+70	+	+
TOTAL CHANGES TO NATIONAL INSURANCE CONTRIBUTIONS	[illegible]	[illegible]	[illegible]3

Will need amendment

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

~~to the basic rate producing~~ a small revenue yield.

21 Legislation will be introduced to make clear the amount of UK tax that is deductible from UK tax credits to which non-residents may be entitled under a double taxation convention. This measure will prevent a potential Exchequer loss of about £15 million a year.

Income tax and corporation tax

22 From 1 January 1990, the rules for taxing life assurance companies will be changed:

to allow relief for the expenses of pension, general annuity and other life assurance business only against their respective profits;

to spread the relief for the costs of acquiring new business (other than pension and general annuity business) over seven years, subject to transitional arrangements in the first four years to phase out the present immediate relief; and

to reduce the corporation tax rate on income and capital gains allowable to policyholders to 25 per cent.

The yield in 1990-91 and the immediately following years is reduced by the proposed transitional arrangements, and by the carry-forward of unrelieved expenses from past years. ~~The yield is likely to peak in 1995-96, diminishing thereafter.~~ The yield in all

X

Should we not give ~~[illegible]~~ 'mature' yields before the 'disclaimer'?

years depends on developments in the industry, particularly in the level of new business, and is therefore highly uncertain.

23 The apportionment rules for close companies will be abolished. A higher rate of corporation tax ~~linked~~ equal to the higher rate of income tax of 40 per cent will be introduced for close investment companies which distribute less than a specified percentage of their profits. A close investment company will no longer get tax relief for interest payments, annual payments or management expenses unless these would have been deductible if paid by an individual.

24 The legislation relating to capital allowances for safety expenditure at sports grounds will be amended from 1 January 1989 to take account of the extension of safety certificate requirements to regulated stands at undesignated sports grounds. Minor amendments will be made to the capital allowances legislation to correct defects and anomalies in advance of the consolidation of that legislation.

25 The period for which relief may be available for business expenditure incurred before a trade begins will be increased from three to five years. The cost of this proposal will take some years to build up and could amount of tens of millions of pounds.

26 Subject to consultation, the requirements of the scheme for subcontractors in the construction industry will be reduced, for

ties for late filing gradually over a period of years, leading to the introduction of automatic penalties for all late filing (but not before 1995).

The effect on revenue in subsequent years is expected to be small.

30 From Budget day the existing corporate deep discount legislation in Schedule 4 ICTA 1988 will be widened to include non-variable deep discounted securities issued by non-corporate borrowers. On a sale or redemption the accrued discount will be taxed as income. Any excess or shortfall will be taxed as a capital gain or loss unless the security is exempt from capital gains tax as a qualifying corporate bond. Where deep discounted securities have variable features so that the precise accrued discount at any particular time cannot be determined in advance (including certain index linked bonds), the whole of the uplift between cost price and sale or redemption price will be taxed as income. The eventual yield is ~~very~~ uncertain but is estimated at around £50 million.

31 A tax charge will be imposed on UK investors on gains when they switch holdings within an offshore fund.

Corporation Tax

32 The profits limit for the small companies' corporation tax rate of 25 per cent for financial year 1989 will be raised from £100,000 to £150,000 and the limit for

BUDGET SECRET
BUDGET LIST ONLY
NOT TO BE COPIED

78 Criminal sanctions will be provided against unlawful disclosure of information relating to an identifiable taxpayer by employees or former employees of revenue departments.

National Insurance Contributions

79 From 1 October 1989, the £75 earnings limit for Class 1 employee contributions will be turned into a threshold and the 7 per cent employee band between £75 and £115 will be abolished.

80 From 1 October 1989, the Upper Earnings Limit will be increased from £325 to £355 a week. The yield (£ million) breaks down as follows:

	1989-90	1990-91
Employees	+110	+350
Employers	-40	-120
Total	+70	+230

Negative yield from employers reflects higher contracted out rebate. 1990-91 costing reflects higher corporation tax yield.

To be re-done

FSBR

BUDGET SECRET

COPY NO. 20 OF 32 COPIES

FROM: J. ANSON
24th February, 1989.

CHANCELLOR

c.c. Chief Secretary
Financial Secretary
Paymaster General
Economic Secretary
Sir P. Middleton
Sir T. Burns
Mr. Wicks
Mr. Scholar
Mr. Culpin
Mrs. Lomax
Mr. Sedgwick
Mr. Riley
Mrs. Butler
Mr. S. Davies
Mr. Gilhooly
Mr. Mowl
Mr. Macpherson
Miss Simpson
Miss Wallace
Mrs. Chaplin
Mr. Tyrie
Mr. Call

Sir Anthony Battishill
Mr. Beighton
Mr. Isaac
Mr. Painter
Mr. Calder

Mr. Unwin
Mr. Jefferson-Smith

MP

FSBR CHAPTER 1

Mr. Riley's submission of 23rd February offers 4 variants of Table 1.1. Could I cast my vote for variant 1 or 3. If an item is important enough to be shown in this table I think we have to show its cost and not just a row of dots. In that case, given that it would be misleading to add it to the other items, it is better to put it below the line as proposed in variants 1 or 3.

JA

J. ANSON

gep.md/feb/ja27

FROM: MRS R LOMAX
DATE: 27 FEBRUARY 1989

MR ANSON

cc: Mr Mowl
Mr Gieve
Mrs Butler
Mr MacAuslan

FSBR TABLE 1.2

You will have seen Mr Gieve's suggestion that the expenditure figures in Table 1.2 be put on functional rather than a departmental basis. We in GEP do not like this. For one thing, we could not provide an up-to-date estimate of this year's outturn on a functional basis. For another, we could not follow this approach next year (since we will not be able to provide plans for the new planning total on a meaningful functional basis). More generally,, the key focus in both Estimates and the Public Expenditure White Paper is on the departmental presentation, and we think it would be confusing to provide figures on a different basis in the FSBR. And because of all this it is surely simpler for briefing purposes too - quick questions can be referred direct to Departments.

2. As for the misleading heading to Table 1.2, that is easily remedied by adding the words "by department" after (or under) expenditure.

RL

RACHEL LOMAX

Mrs Lomax — as before

PPS

I ~~know~~ can't see that using a functional split in the FSBR will confuse anyone. When we are presenting documents to Parliament as a basis for their scrutiny of departments, it makes sense to use a departmental split. But where we are trying to give a brief overview of how the money is spent, the functional division makes more sense.

4/2 Next year we will have to recast the table in any event to take account of CG grants to LAs & LA's projected self financed expenditure. It may be best at that stage to divide it out into CG, LAs & PCs

JG

gep.md/feb/ja27

FROM: MRS R LOMAX
DATE: 27 FEBRUARY 1989

MR ANSON

cc: Mr Mowl
Mr Gieve
Mrs Butler
Mr MacAuslan

FSBR TABLE 1.2

You will have seen Mr Gieve's suggestion that the expenditure figures in Table 1.2 be put on functional rather than a departmental basis. We in GEP do not like this. For one thing, we could not provide an up-to-date estimate of this year's outturn on a functional basis. For another, we could not follow this approach next year (since we will not be able to provide plans for the new planning total on a meaningful functional basis). More generally,, the key focus in both Estimates and the Public Expenditure White Paper is on the departmental presentation, and we think it would be confusing to provide figures on a different basis in the FSBR. And because of all this it is surely simpler for briefing purposes too - quick questions can be referred direct to Departments.

2. As for the misleading heading to Table 1.2, that is easily remedied by adding the words "by department" after (or under) expenditure.

RL

RACHEL LOMAX

cc. PPS
PS/CST
as before.

Mrs Lomax

I agree. It would be helpful to include your amendment in the heading.

JA 28/2

idt.lp.division.8

FROM: J GIEVE
DATE: 27 FEBRUARY 1989

MR MOWL

cc Chancellor
Chief Secretary
Mr Anson
Mrs Lomax
Ms Simpson

FSBR TABLE 1.2

I like the new format of Table 1.2 but I think it would be further improved if the expenditure figures were on a functional rather than a departmental basis ie that the social security figure was the total cost of social security in the UK rather than the DHSS budget, that health showed the total cost of the NHS rather than expenditure on health and personal social services in England and so on. At present the headings are misleading not only on those point but, for example, in suggesting that total spending in Scotland is £8.5 billion. While there are good grounds of accountability for organising our Estimates and other public expenditure publications by department, I think the functional analysis gives a clearer picture of 'what the money is spent on' for FSBR purposes.

2. The necessary figures are set out in Table 21.1.7 of the Public Expenditure White Paper. To keep the same number of lines, you might substitute Law and Order, Transport, Housing and Environment, Industry etc, and Overseas for the lines presently given to Home Office, Transport, Scotland, Wales, and Northern Ireland. There would be a consequential amendment to para 610.

JG. Gieve

JOHN GIEVE

chex.ps/aa/7

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

REF NO. ACSA/89/10
COPY NO. 21 OF 32.

FROM: A C S ALLAN
DATE: 27 February 1989

MR RILEY

Mp

cc PS/Chief Secretary
PS/Financial Secretary
PS/Paymaster General
PS/Economic Secretary
Sir P Middleton
Sir T Burns
Mr Anson
Mr Wicks
Mr Scholar
Mr Culpin
Mrs Lomax
Mr Sedgwick
Mrs Butler
Mr S Davies
Mr Gilhooly
Mr Mowl
Mr Macpherson
Miss Simpson
~~Miss Wallace~~
~~Mrs Chaplin~~
Mr Tyrie
Mr Call

Sir A Battishill - IR
Mr Beighton - IR
Mr Isaac - IR
Mr Painter - IR
Mr Calder - IR
Mr Unwin - C&E
Mr Jefferson Smith - C&E

FSBR CHAPTER 1

The Chancellor was grateful for your minute of 23 February. I attach a copy of the draft with his comments marked.

2. He would prefer to use Varient 2 of the four versions of Table 1.1: he noted Mr Anson's vote, but felt that including figures for the abolition of the pensioners' earnings limit in the table provided too great a temptation to others to add that in to produce a spurious total. He does, however, feel that the (gross) public expenditure cost should be shown in the footnote.

ACSA

A C S ALLAN

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

<chapter> 1 The Budget

1.01. The objective of the Government's economic policy is to defeat inflation and to maintain a vigorous and enterprising economy, with sustained growth of output and increased employment.

1.02. The Financial Statement and Budget Report (FSBR) supplements the Chancellor's Budget Statement. It presents the Medium Term Financial Strategy (MTFS); describes developments in the economy over the past year; provides forecasts to mid-1990; sets out the tax proposals in the Budget; summarises the Government's spending plans; and gives forecasts for the public finances for the year ahead.

<side> **The Medium Term Financial Strategy**

1.03. Chapter 2 describes the MTFS, which provides the framework for the Government's economic policy. The objectives of the MTFS and the central role of monetary policy have remained unchanged throughout the 1980s, a period of substantial economic progress. Monetary policy is designed to ~~bring down~~ reduce the growth of money GDP over the medium term, so bringing down inflation. It is

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

~~[conducted within a sound fiscal framework]~~; in this year's MTFS a gradual return to ~~budget~~ a balanced Budget is projected over the medium term, with both taxes and public expenditure declining as a share of GDP. The MTFS is complemented by policies designed to improve the working of markets and the supply performance of the economy.

buttressed by a sound fiscal policy, with a substantial Budget surplus in both 1988-89 and 1989-90;

<side> **The economy**

1.04. Chapter 3 describes the main developments in the economy in 1988 and the prospect until mid-1990. In recent years ~~developments~~ economic trends have ~~been~~ become increasingly difficult to interpret because of inconsistencies within the national and sectoral accounts; adjusted figures that reduce (but do not eliminate) these inconsistencies are used throughout the FSBR. The economy grew strongly again in 1988, with the largest fall in unemployment since the war. GDP is forecast to grow by a further 2½ per cent in 1989, ~~though~~ on the basis of growth through the year ~~is forecast to be lower.~~ lower than this. Inflation ~~should~~ is forecast to be on a downward trend ~~again~~ in the second half of 1989.

<side> **Tax and National Insurance measures**

1.05. Chapter 4 sets out the tax and National Insurance proposals in the Budget. They include indexation of the main income tax allowances, abolition of stamp duty on shares, improvements to personal equity plans and employee share schemes, reform of the taxation of life assurance, pensions, and unit trusts, measures to promote unleaded petrol, ~~simplification and deregulation of VAT,~~ ~~and~~ reform and reduction of employee National Insurance contributions, together with abolition of the earnings rule for pensioners. The measures are summarised in table 1.1.

<side> **Public expenditure**

1.06. Chapter 5 summarises the Government's spending plans, as set out in the public expenditure White Paper. This chapter also provides the latest estimate of the outturn for the public expenditure planning total in 1988-89.

BUDGET SECRET
BUDGET LIST ONLY
NOT TO BE COPIED

<side> **Public sector finances**

1.07. Chapter 6 presents the complete financial picture for the public sector. The public sector debt repayment is forecast to be [£14 billion] in 1988-89. A further debt repayment of [£12 billion] is forecast for 1989-90, equivalent to £7 billion net of privatisation proceeds, the same as in 1988-89. The forecast takes account of the measures in the Budget which are expected to reduce taxation and National Insurance contributions by £1.9 billion, after adjusting for the net cost of indexing direct and indirect tax rates and allowances. Table 1.2 shows the main components of general government receipts and expenditures.

[no comment on this page]

fp.nh/sf/42

VARIANT 2

TABLE 1.1 THE BUDGET MEASURES[1]

£ million yield (+)/cost (-)

	1989-90 Changes from a non-indexed base	1989-90 Changes from an indexed base	1990-91 Changes from an indexed base
Income Tax			
personal allowances and basic rate limit indexed	-1465	-	-
car benefit scales increased	+ 90	+ 90	+ 110
Schedule E put on receipts basis	- 60	- 60	- 80 May be dropped
Excise duties			
petrol, derv etc	-	- 545	- 580
duty on unleaded petrol reduced, surcharge added to 2 star petrol	- 30	- 30	- 75
vehicle excise duty	+ 40	- 150	- 170
tobacco	-	- 235	- 250
alcohol	-	- 255	- 280
Value Added Tax			
non- domestic construction etc	+ 315	+ 315	+ 540
bad debt relief, reform of registration rules etc	- 105	- 105	- 270
Stamp duty on shares abolished	+ 10	+ 10	- 900
Life assurance businesses' tax regime reformed	- 20	- 20	+ 45
~~Reforms to pensions, personal equity plans, share schemes and unit trusts~~	~~- 5~~	~~- 5~~	~~- 10~~
Corporation Tax			
small companies' rate threshold increased	*	*	- 35
Other tax changes	~~- 70~~ -75	~~- 35~~ -40	~~+ 25~~ +15
National Insurance Contributions	- 860	- 860	-2400
Pensioners' earnings limit abolished[2]	..	..	..
Total	-2160	-1885	-4370

1 These measures, and the basis of the costings shown, are described in detail in chapter 4.

2 Public expenditure cost At £250m will be met from the Reserve. See Chapter 5.

chex.ps/aa/6

BUDGET - SECRET
BUDGET LIST ONLY

REF NO. ACSA/89/12
COPY NO. 1 OF 30.

FROM: A C S ALLAN
DATE: 27 February 1989

MR MOWL

cc PS/Chief Secretary
PS/Financial Secretary
PS/Paymaster General
PS/Economic Secretary
Sir P Middleton
Sir T Burns
Mr Anson
Mr Wicks
Mr Scholar
Mr Sedgwick
Mr Riley
Mr Culpin
Mrs Lomax
Mr S J Davies
Mr Hibberd
Mrs R Butler
Mr Pickford
Mr Gieve
Mr Patterson
Mrs Wright
Mrs Todd
Miss Simpson
Mrs Chaplin
Mr Tyrie
Mr Call

Mr Calder - IR
Mr Vernon - C&E

FSBR TABLE 1.2 AND CHAPTER 6

The Chancellor was grateful for your minute of 22 February and the draft of Chapter 6, which he thought read well. I attach a copy of the draft with his comments marked.

2. He had several comments on the charts:

(i) he is content for the charts showing the GGE ratio and non-oil tax burden to start in 1978-79;

(ii) in Chart 6.1 he would prefer the non-oil line unbroken and the total line broken;

(iii) he would prefer Chart 6.3 (on debt interest payments) redone as a percentage of GDP;

(iv) he would like Chart 6.4 (on sectoral borrowing requirements) redone: it should be turned upside down, so that repayments are shown above the line and borrowings below it; the overall PSBR column should be dropped; the area above the line should be labelled "Repayment" and that below the line labelled "Borrowing";

(v) he would like Charts 6.5 and 6.6 omitted; but he would like to reinstate the equivalent of last year's Chart 6.2.

ACSA

A C S ALLAN

COPY NO: 30 of 30 copies + 1

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

Table 1.2[1] The finances of the Public Sector

	£ billion 1988-89 1988 Budget	1988-89 Latest estimate	1989-90 Forecast
RECEIPTS			
Inland Revenue:			
Income tax	42.1	43.5	47.1
Corporation tax[3]	19.8	18.8	22.0
Petroleum revenue tax	1.2	1.3	1.3
Capital gains tax	2.0	2.4	2.1
Inheritance tax	1.0	1.1	1.1
Stamp duties	2.0	2.3	2.6
Total Inland Revenue	**68.0**	**69.4**	**76.1**
Customs and Excise:			
Value added tax	26.2	27.5	29.8
Petrol, derv duties etc	8.4	8.7	8.7
Tobacco duties	5.0	5.1	5.1
Alcohol duties	4.5	4.6	4.7
Betting and gaming duties	0.9	0.9	0.9
Car tax	1.3	1.4	1.4
Customs duties	1.6	1.7	1.8
Agricultural levies	0.1	0.2	0.1
Total Customs and Excise	**47.9**	**49.9**	**52.5**
Vehicle excise duties	2.8	2.8	2.9
Oil royalties	0.6	0.6	0.6
Gas levy	0.4	0.4	0.4
Local authority rates[4]	19.0	18.9	20.4
Other taxes and royalties	2.5	2.7	2.8
Total taxes and royalties	**141.2**	**144.8**	**155.7**
National insurance and other contributions	31.6	32.8	34.6
Interest and dividends	5.6	6.6	6.7
Gross trading surpluses and rent	3.5	3.3	3.5
Other receipts	2.9	3.3	3.3
General Government Receipts	**184.9**	**190.8**	**203.7**

	£ billion 1988-89 1988 Budget	1988-89 Latest estimate	1989-90 Forecast
EXPENDITURE			
Social security	48.5	47.4	51.0
Health	20.7	21.8	23.2
Defence	19.2	19.0	20.1
Education and science	18.0	18.4	19.6
Home office and legal departments	7.0	7.2	8.0
Transport	5.1	4.8	5.4
Scotland	8.5	8.7	9.0
Wales	3.5	3.6	3.8
Northern Ireland	5.1	5.6	5.5
Other departments	22.8	21.7	23.1
Privatisation proceeds	-5.0	-7.0	-5.0
Reserve	3.5	-	3.5
Public expenditure planning total	**156.9**	**151.1**	**167.1**
General government gross debt interest	17.5	18.2	16.6
Other adjustments	8.6	9.2	9.5
General Government Expenditure	**183.0**	**178.5**	**193.2**

Receipts, expenditure and debt repayment

	£ billion 1988-89 1988 Budget	1988-89 Latest estimate	1989-90 Forecast
General government receipts	184.9	190.8	203.7 8
General government expenditure	183.0	178.5	193.2
General government debt repayment	2.0	12.3	10.5 6
Public corporations' market and overseas debt repayment	1.2	1.7	1.5
Public sector debt repayment	**3.2**	**14.0**	**12.0** 1

1 In this and other tables constituent items may not add up to totals because of rounding.
~~2 On current definitions.~~
3 Includes advance corporation tax (net of repayments): 5.3 6.0 6.4
- also includes North Sea corporation tax after ACT set off and corporation tax on gains.
4 In this and other tables community charge receipts in Scotland are included with local authority rates.

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

<chapter> 6 The public sector's ~~finances~~

<side> The scope of this chapter

6.01. This chapter brings together revenue and spending and provides an analysis and forecast of the public sector's overall financial position in 1989-90, together with some explanation of the main differences between estimated outturn in 1988-89 and last year's forecast.

<side> Debt repayment

6.02 The latest estimate is for a public sector debt repayment (PSDR) of £14 billion in 1988-89, equivalent to 3 per cent of GDP, ~~This is~~ a larger net repayment as a proportion of GDP than in any year since the beginning of the 1950s - the earliest date for which comparable figures are available ~~- even if privatisation proceeds are excluded. In 1988-89 all the main fiscal indicators - the PSDR, the PSDR excluding privatisation proceeds,~~ Both the public sector financial ~~deficit~~ balance ~~(PSFD)~~ and the general government financial ~~deficit - will be~~ balance in substantial surplus.

or £7 billion excluding privatisation proceeds.

Even this last represents

are also estimated to be

6.03 The forecast is for a further substantial PSDR of around £12 billion in 1989-90. Excluding privatisation proceeds the PSDR is forecast to be the same in 1989-90 as in 1988-89.

Table 6.1 Public sector debt repayment

	£ billion and as per cent of GDP			
	1987-88	1988-89		1989-90
	Outturn	1988 Budget	Latest estimate	Forecast
Public sector debt repayment				
£ billion	3.5	3.2	14.0	12.0
as per cent of GDP	¾	¾	3	2¼
PSDR excluding privatisation proceeds				
£ billion	-1.6	-1.8	7.0	7.0
as per cent of GDP	-½	-½	1½	1¼ ? 1½

6.04. The stock of net public sector debt has fallen from over 50 per cent of money GDP in 1979 to 38½ per cent (£171 billion) at the end of 1987-88. It is ~~estimated~~ forecast to be about £[157] billion, or [31½] per cent of GDP, at the end of 1988-89. There should be a further large fall in 1989-90, in both nominal terms and as a percentage of GDP.

X

– the lowest figure for X years.

<section> **Changes since last Budget**

6.05 The PSDR in 1988-89 is now estimated to be nearly £11 billion higher than forecast in last year's Budget. As table 6.2 shows the higher net repayment comes roughly equally from higher receipts and lower expenditure, including £2bn additional privatisation proceeds (see table 1.2 for a detailed comparison of the components). Much of the extra receipts reflects the higher than forecast growth of money GDP. Higher growth has also contributed to the lower than forecast expenditure, primarily through lower ~~than expected expenditure~~ spending on social security and improved finances of public corporations.

Table 6.2 Changes to receipts, expenditure and debt repayment since 1988 Budget[1]

	£ billion 1987-88	1988-89
Receipts		
Taxes, royalties and national insurance contributions	+0.8	+4.8
Other receipts	-0.7	+1.1
Total	+0.2	+5.9
Expenditure		
Privatisation proceeds	-0.1	-2.0
Other general government	+0.2	-2.4
Public corporations' market and overseas finance	-0.4	-0.6
Total	-0.3	-5.0
PSDR	+0.5	+10.8

1 + higher receipts, ~~or~~ higher expenditure; or higher debt repayment;
\- lower receipts or lower expenditure.

6.06. The main contributors to the higher than expected receipts are income tax (£1½ billion), national insurance contributions (£1 billion), VAT (£1¼ billion) and interest receipts (£1 billion). The first two largely reflect higher total wages and salaries. Higher VAT receipts are the result of faster growth of consumer spending in total and a change in its composition towards those goods and services which are subject to VAT.

6.07. Corporation tax receipts again rose strongly in 1988-89 but not by as much as forecast. Within the total, advance corporation tax (ACT) receipts were higher than forecast, reflecting high dividend payments in 1988, but other corporation tax receipts rose much less than expected. The latter is likely to be mainly the result of lower profits and higher investment in 1987 than shown by the recorded figures available at the time of the last Budget.

Please check: is this true?

Privatisation proceeds were £2 billion higher than projected at the time of

6.08. ~~On the expenditure side higher privatisation proceeds reduced expenditure by £2 billion compared with~~ the last Budget. ~~But~~ expenditure excluding privatisation proceeds ~~is also~~ was lower than forecast, largely as a result of lower ~~than projected~~ social security expenditure and higher ~~than expected~~ local authority capital receipts.

6.09. The public sector's finances can be analysed in a number of different ways: by type or activity, by sector and by economic category. The rest of this chapter sets out these three analyses in detail.

<section> **Public sector's finances: analysis by type or activity**

6.10. Table 1.2 analyses the public sector's finances by type or activity. The main receipts of general government (ie. central plus local government) are grouped according to the kind of activity which gives rise to them, while spending is shown by department, as in Chapter 5 and in the public expenditure White Paper.

<side> **Receipts**

6.11. General government receipts are estimated to have risen by 9½ to 10 per cent in 1988-89, just below the growth of money GDP. They are forecast to rise by 6½-7 per cent in 1989-90, a little less than the forecast growth of money GDP.

6.12. North Sea revenues are forecast to fall by 15 per cent in 1989-90, mainly the delayed effect on corporation tax of falling profits in earlier years. Oil production is expected to be lower in 1989 than in 1988, due mainly to the continued effect of the Piper Alpha disaster and accidents in the Fulmar and Brent fields. The forecast assumes that North Sea oil prices will remain close to recent levels. PRT receipts are forecast to be the same in 1989-90 as in 1988-89 despite the projected fall in production because there were repayments of advance PRT in 1988-89 and none are forecast for 1989-90. [~~A $1 a barrel difference in the average oil price in 1989 would change revenues by about £210 million in 1989-90 and £270 million in a full year. A change of 1 million tonnes in oil production in 1989, spread evenly across fields, would alter revenues by about £35 million in 1989-90 and £40 million in a full year.~~]

Table 6.3 North Sea revenues

	£ billion			
	1987-88	1988-89		1989-90
	Outturn	1988 Budget	Latest Estimate	Forecast
North Sea corporation tax[1]	1.4	1.5	1.3	0.8
Petroleum revenue tax[2]	2.3	1.2	1.3	1.3
Oil royalties	1.0	0.6	0.6	0.6
Total North Sea revenues	**4.7**	**3.3**	**3.2**	**2.7**
[1] before ACT set off of:	0.7	0.8	0.8	0.5

[2] includes advance petroleum revenue tax

6.13. Excluding North Sea revenues general government receipts rose by over 10½ per cent in 1988-89 and ~~are~~ forecast to rise by about 7 per cent in 1989-90. Within ~~the~~ this overall increase forecast for 1989-90 there is:

an 8 per cent increase in income tax receipts;

an 18 per cent increase in non-oil corporation tax, with ACT growing more slowly than the rest;

an 8 per cent increase in VAT receipts, a little less than the increase in consumers' expenditure, reflecting relatively slow growth of ~~the component~~ spending subject to VAT;

little change in receipts from the excise duties on petrol, tobacco and alcohol; ~~following the freeze of duty rates announced in the Budget~~;

an 8 per cent increase in local authorities' net receipts of rates (and community charge in Scotland);

a 5½ per cent increase in national insurance contributions, after allowing for the reforms to employees' contributions announced in the Budget.

<side> Taxes as a share of GDP

6.14. Table 6.4 shows total taxes ~~(including rates and community charge)~~ and national insurance contributions (NICs) as a percentage of GDP. Both the total and non-oil percentages are estimated to have fallen in 1988-89, by about ½ percentage point in each case, compared with a forecast of no change in last year's Budget. Given the payments lags in the tax system a fall in the percentage is likely when there is a pick-up in the growth of money GDP. Some taxes, such as mainstream corporation tax, are paid some time after the period for which the liability is incurred. For over 20 per cent of total tax receipts the payments lags are one year or longer; receipts of these taxes are therefore ~~invariant to~~ unaffected by changes in GDP in the same year. With other taxes, stamp duty for example, there is a variable relationship between changes in the tax base and changes in money GDP.

X

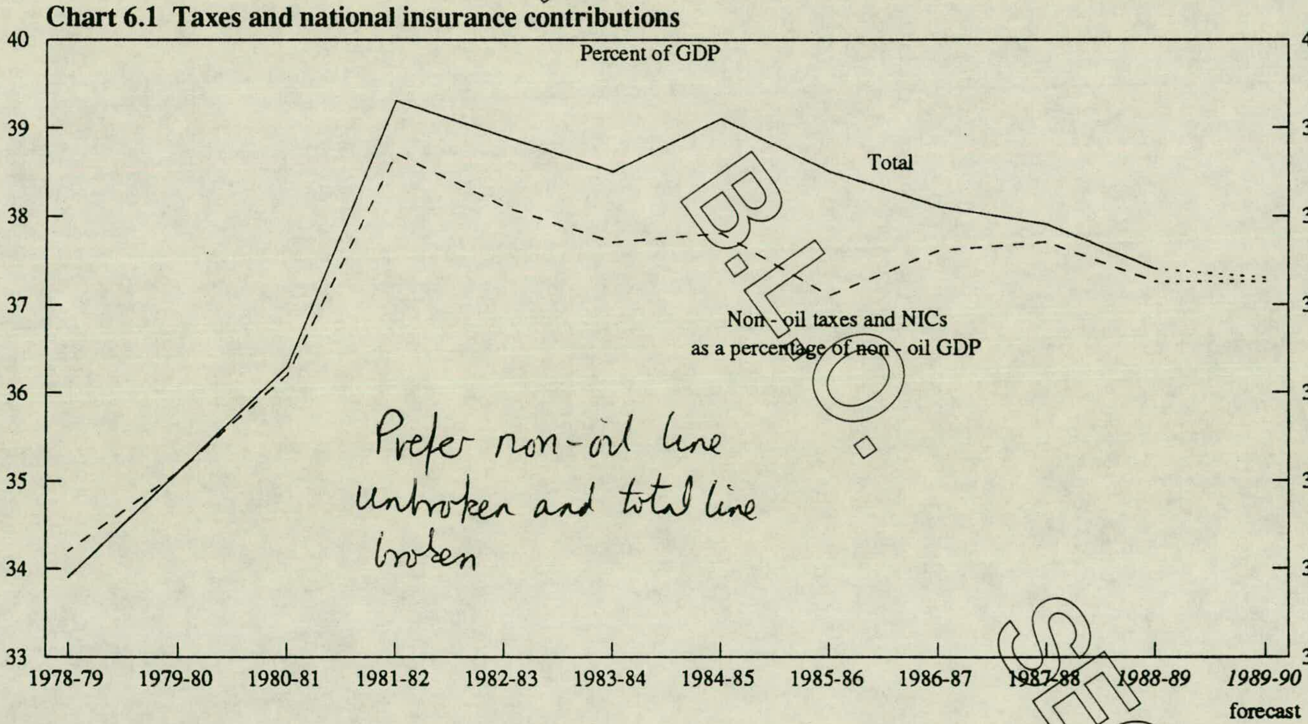
6.15. The forecast is for non-oil taxes and NICs to be the same as a percentage of money GDP in 1989-90 as in 1988-89. Real fiscal drag - the tendency for average tax rates to rise

In other words, the changes in the Budget merely offset in a progressive tax system indexed to price changes, ~~would be expected to increase the percentage but in 1989-90 the effect of this is largely offset by the additional effect in 1989-90 of the 1988 Budget and by the tax changes in this year's Budget.~~ With the projected fall in North Sea revenues in 1989-90, total taxes and NICs are forecast to fall slightly as a percentage of GDP, ~~in that year.~~

Table 6.4 Taxes and national insurance contributions as a percentage of GDP

	1983-84	1984-85	1985-86	1986-87	1987-88	1988-89 Latest estimate	1989-90 Forecast
Total taxes and NICs as a share of total ~~money~~ GDP	38.5	39.1	38.5	38.1	37.9	37.4	37.2
Non-oil taxes and NICs as a share of non-oil ~~money~~ GDP	37.7	37.8	37.1	37.6	37.7	37.3	37.3

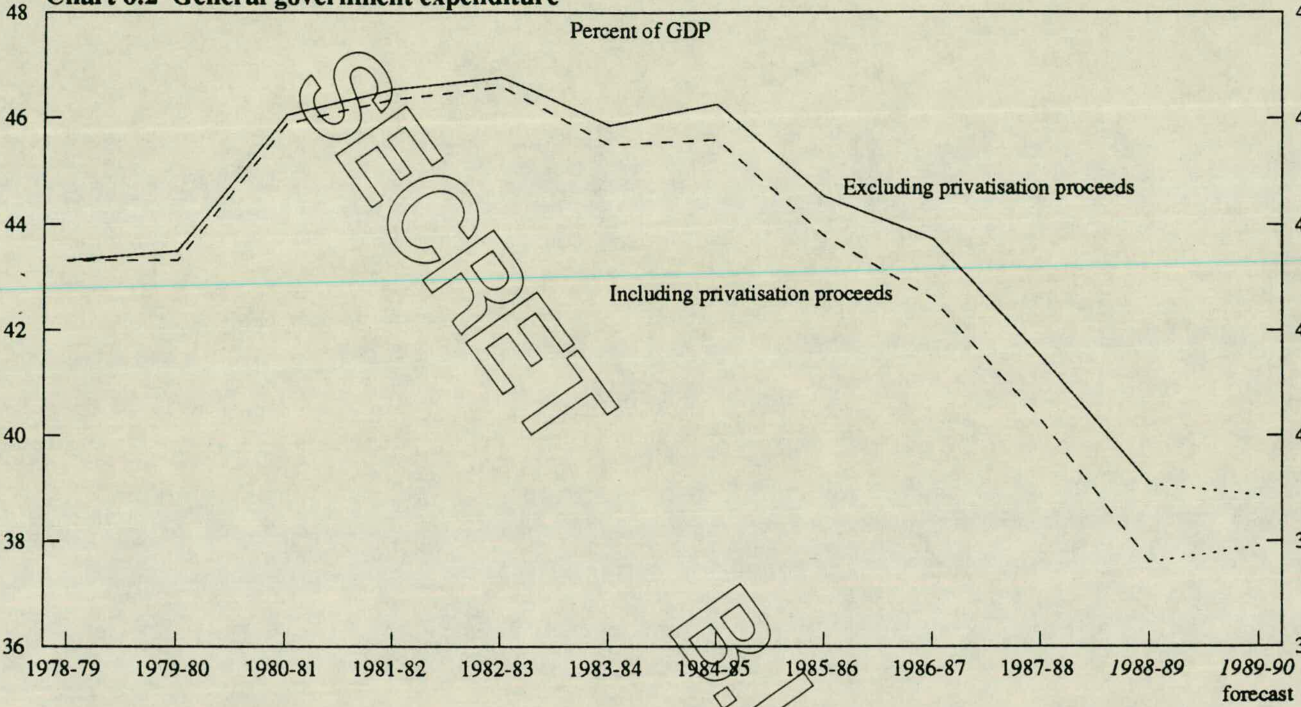
Chart 6.1 Taxes and national insurance contributions



<side> **Expenditure**

6.16. General government expenditure (GGE) excluding privatisation proceeds is now estimated to have increased by under 5 per cent in 1988-89, and is forecast to rise by nearly 7 per cent in 1989-90, below the growth of money GDP in both years. The ratio of GGE excluding privatisation proceeds to money GDP is therefore expected to fall~~s~~ in both years, as illustrated in chart 6.2.

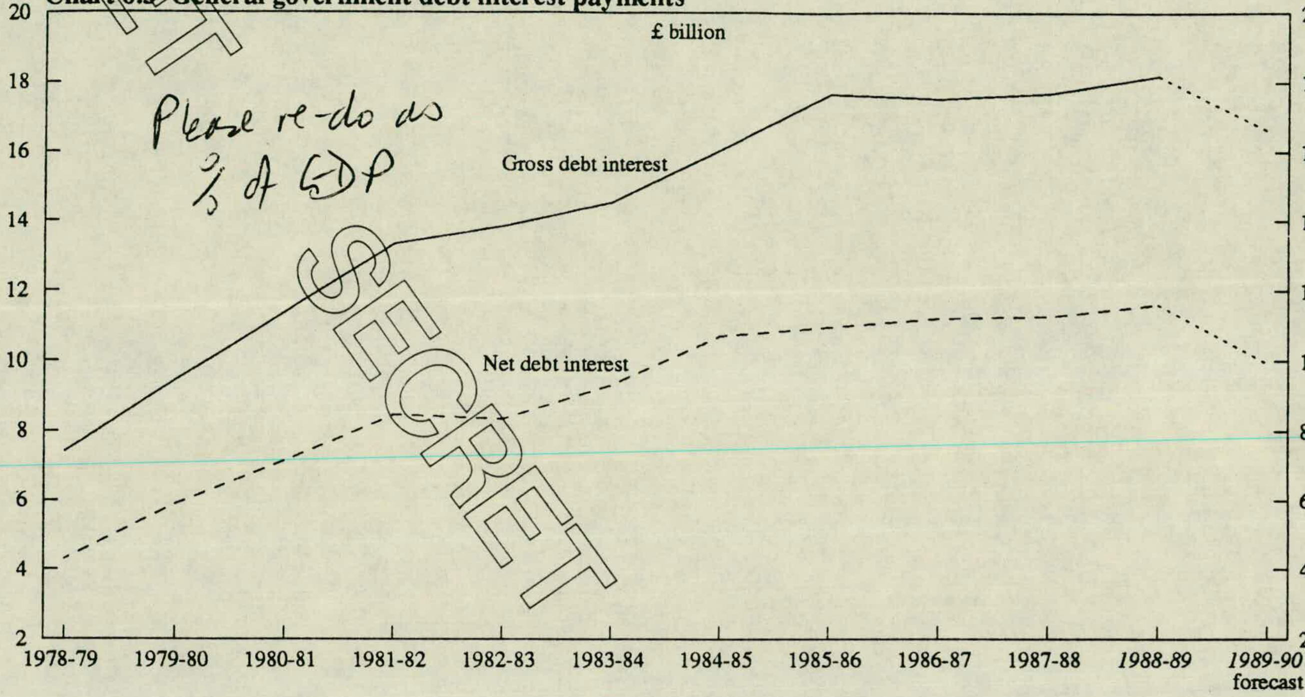
Chart 6.2 General government expenditure



6.17. Within GGE, gross debt interest payments rose in cash terms in 1988-89 partly because of higher interest rates and inflation (which raises the cost of servicing indexed debt). Net debt repayment reduces interest payments, other things being equal, but not immediately; and because of the rise in the foreign exchange reserves and other short-term assets in 1987-88 and early 1988-89 some of the effect has come through initially as higher interest receipts. Interest and dividend receipts rose by £½ billion in 1988-89, despite a fall in the dividend element following the sale of the Government's remaining shareholding in BP.

6.18. Gross debt interest payments are forecast to fall substantially in 1989-90, against a background of no change in interest and dividend receipts.

Chart 6.3 General government debt interest payments



Please re-do in debt repayment terms (reversing all signs) to make consistent with rest of Chapter

<section> **Public sector's finances: analysis by sector**

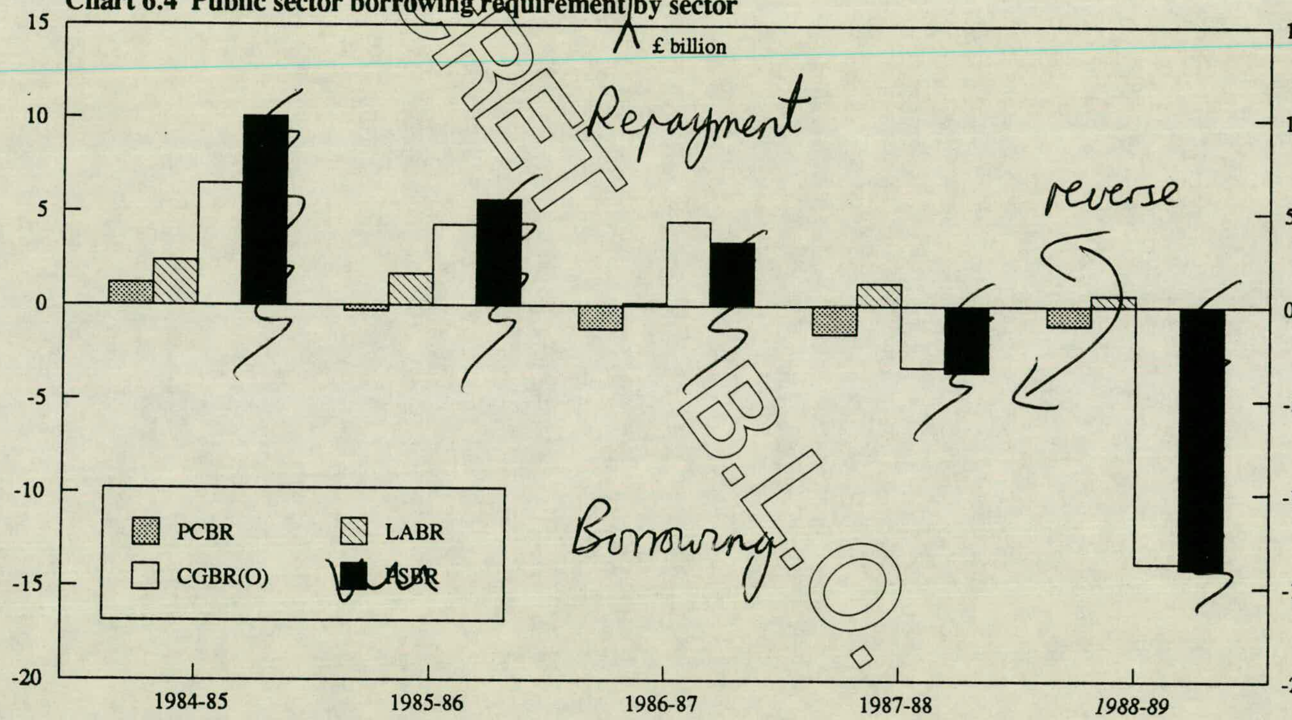
6.19. Table 6.5 shows net borrowing in 1987-88 and 1988-89 by central government, local authorities and public corporations.

Table 6.5 Public sector borrowing requirement

	£ billion	
	1987-88 Outturn	1988-89 Latest estimate
1 Central government borrowing on own account	**-3.2**	**-13.7**
2 Local authority borrowing from central government	4.1	4.5
3 Local authority borrowing from market and overseas	-2.9	-3.9
4 Total local authority borrowing	**1.2**	**0.6**
5 Public corporations' borrowing from central government	0.0	0.8
6 Public corporations' borrowing from market and overseas	-1.5	-1.7
7 Total public corporations' borrowing	**-1.5**	**-1.0**
8 Public sector borrowing requirement	**-3.5**	**-14.0**
Central government borrowing requirement (lines 1+2+5)	0.9	-8.5

6.20. The ~~PSBR~~ PSDR in the first ten months of 1988-89, a net repayment of £15.5 billion, was substantially ~~lower~~ higher than in the same period of 1987-88, both including and excluding privatisation proceeds. The ~~larger~~ greater part of the ~~reduction~~ increase was ~~in~~ on central government own account. ~~borrowing, but local authority and public corporations' borrowing were also lower than last year~~. Taking into account both further privatisation proceeds of about £1 billion due in March and the well established pattern of ~~positive net~~ high borrowing in March, the forecast for 1988-89 as a whole is a public sector net debt repayment of £14 billion. ~~a somewhat smaller net repayment than recorded for the first ten months of the year~~.

Chart 6.4 Public sector borrowing requirement /debt repayment by sector[1]



1. including privatisation proceeds

6.21. Tables 6.6 to 6.8 show estimated outturns and forecasts of receipts and expenditure in 1988-89 and 1989-90 for each of the three sectors. Expenditure in 1989-90 does not include an allocation of the Reserve, although the forecast of the PSDR assumes that the Reserve is fully spent.

ide> **Central government**

6.22. Central government expenditure in table 6.6 includes grants and subsidies to local authorities and public corporations (including nationalised industries), which are included in the receipts of those sectors, shown in Table 6.7 and 6.8. The forecast large rise in 1989-90 in net lending etc is mainly the result of a lower level of privatisation proceeds.

[no comments on this page]

Table 6.6 Central government transactions

	£ billion 1987-88 Outturn	1988-89 Latest estimate	1989-90 Forecast
Receipts			
Taxes and royalties	115.8	125.9	135.3
National insurance and other contributions	29.0	32.8	34.6
Other	10.4	11.4	10.8
Total receipts	**155.1**	**170.1**	**180.6**
Expenditure			
Current expenditure on goods and services	52.5	56.8	61.5
Current grants and subsidies	80.5	80.0	86.2
Interest	17.2	17.6	16.2
Net lending[1], capital expenditure, and cash expenditure on company securities	1.6	2.0	4.8
Total expenditure	**151.8**	**156.4**	**168.7**[2]
Consolidated Fund revenues	123.0	135.5	141.2

1 Excluding lending to local authorities and public corporations.
2 Excluding any allocation from the Reserve.

<side> **Local authorities**

6.23. Local authority receipts consist primarily of rate income plus grants from central government. The forecast increase in rate income (net of rate rebates) between 1988-89 and 1989-90 takes account of available information about rate decisions by local authorities and additions to rateable value. The forecast of receipts is consistent with the announced levels of community charge in Scotland. The forecast of expenditure in 1989-90 is lower than it would otherwise have been because of the transfer of polytechnics from the local authority to the private sector.

6.24. As chart 6.5 shows the sharp rise in the local authority borrowing requirement (LABR) in 1983-84 and 1984-85 was the result of rising net capital expenditure and a falling current surplus. The subsequent reduction in borrowing is partly associated with rising capital receipts which have reduced net capital spending. From information available about the first ten months it looks as if the (LABR) will turn out to be rather lower in 1988-89 than in 1987-88, ~~again~~ partly due to lower net capital spending, as a result of rising capital spending,

Local authority borrowing requirement

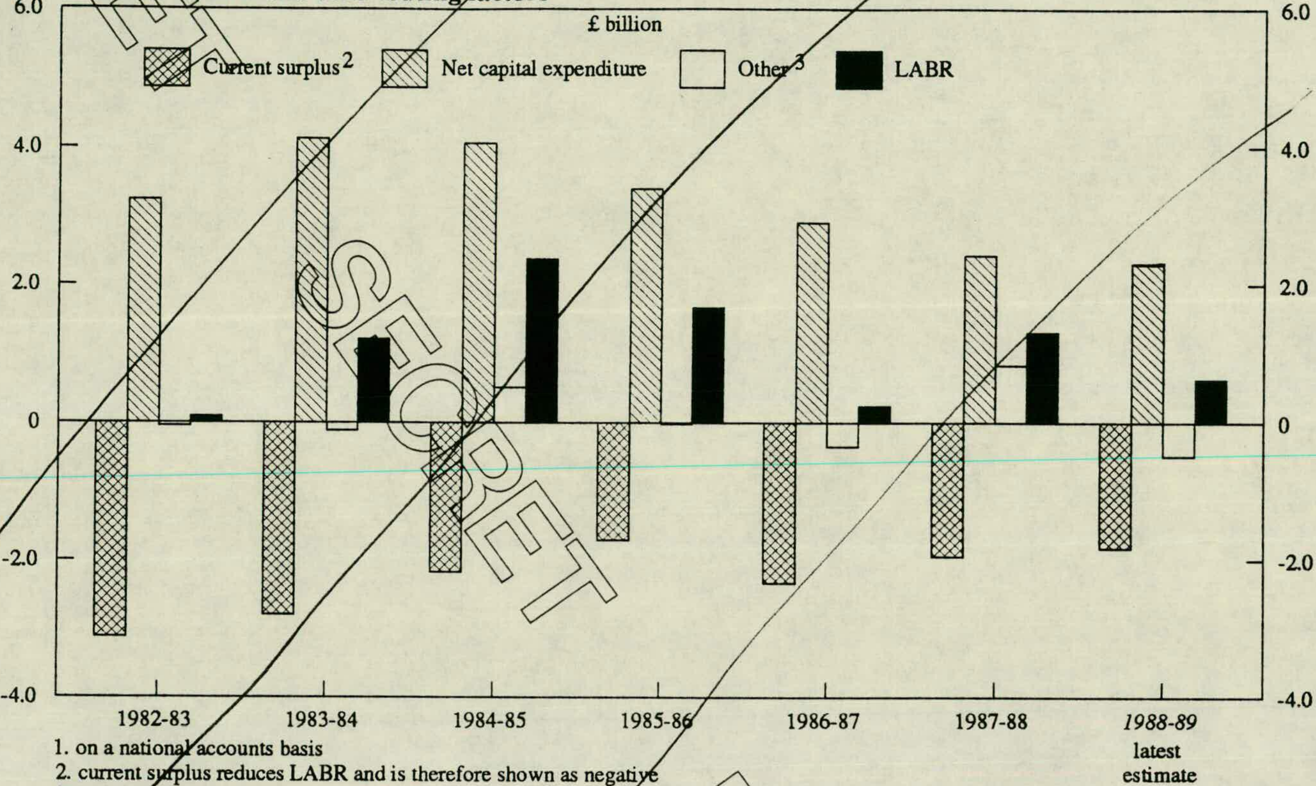
Table 6.7 Local authority transactions

	£ billion 1987-88 Outturn	1988-89 Latest estimate	1989-90 Forecast
Receipts			
Rates and community charge	17.0	18.9	20.4
Rate and revenue support grant	12.5	12.7	13.0
Other grants from central government	12.0	12.2	12.9
Other	5.4	5.9	7.0
Total receipts	**46.9**	**49.7**	**53.3**
Expenditure			
Current expenditure on goods and services	34.6	36.4	37.0
Current grants and subsidies	5.5	6.0	6.8
Interest	4.4	4.7	4.8
Net lending and capital expenditure	3.6	3.3	2.5
Total expenditure	**48.1**	**50.4**	**51.0**[2]

[1] Net of rate rebates: 1.9 1.6 1.6
[2] Excluding any allocation from the Reserve.

OMIT

Chart 6.5 LABR and contributing factors[1]



1. on a national accounts basis
2. current surplus reduces LABR and is therefore shown as negative
3. mainly balancing item

<side> **Public corporations**

6.25. Table 6.8 shows public corporations' transactions. The public corporations' receipts include subsidies and capital grants from central and local government. Changes in public corporations' income and expenditure from one year to another are affected by privatisations which involve re-classifying privatised industries from the public to the private sector in the national accounts. For example the 12 per cent increase in gross trading surplus in 1988-89 would have been larger had British Steel not been excluded, following its privatisation. ~~from the figures for the last quarter, and gross trading surplus would have been forecast to increase more in 1989-90.~~

Table 6.8 Public corporations' transactions

	£ billion		
	1987-88 Outturn	1988-89 Latest estimate	1989-90 Forecast
Receipts			
Gross trading surplus (including subsidies)	6.8	7.6	8.1
Other	2.4	2.0	2.6
Total receipts	**9.2**	**9.6**	**10.7**
Expenditure			
Interest, dividends and taxes on income	3.1	3.3	3.6
Net lending and capital expenditure	4.5	5.4	5.8
Total expenditure	**7.6**	**8.6**	**9.4**[1]

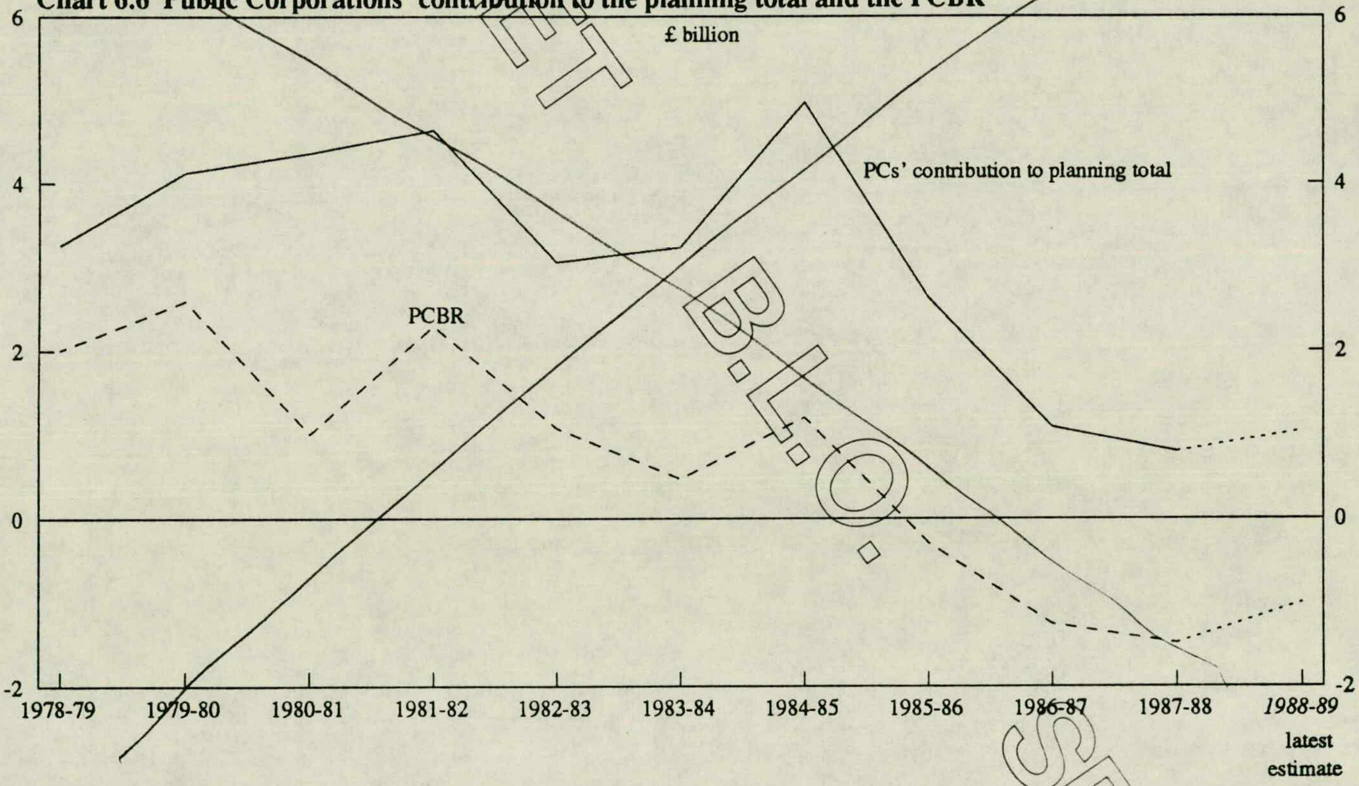
Public corporations' contribution to planning total:

nationalised industries' external finance	0.3	0.4	0.0
other public corporations	0.5	0.6	0.9

[1] Excluding any allocation from the Reserve

OMIT

Chart 6.6 Public Corporations' contribution to the planning total and the PCBR



<section> **Public sector's finances: analysis by economic category**

6.26. The full analysis of receipts and expenditure by economic category is shown in Table 6.9, with a breakdown between central government, local authorities and public corporations. This analysis, which distinguishes between current and capital transactions (and within the latter between physical and financial investment), shows the derivation of the public sector financial surplus ~~deficit~~. The financial surplus ~~deficit~~, unlike X the PSDR ~~PSBR~~, is not wholly a measure of cash transactions because certain items above line 24 in Table 6.9, for example some taxes included in lines 1 and 2, are measured on an accruals basis. An accruals adjustment is accordingly made in line 28.

6.27. The unallocated Reserve is assumed to be on current spending items or physical capital formation ie. in transactions that fall above the financial surplus ~~deficit~~ line. In practice allocations from the Reserve can affect financial transactions (lines 25 to 29).

Table 6.9 Public sector transactions by sub-sector and economic category

£ billion
1988-89 Latest estimate

	Line[1]	General government: Central govern-ment	Local authori-ties	Total	Public corpora-tions	Public sector
Current and capital receipts						
Taxes on income, and oil royalties	1	62.8	-	62.8	-0.2	62.6
Taxes on expenditure~~, and community charge~~ (2)	2	57.9	18.9	76.7	-	76.7
Taxes on capital	3	5.2	-	5.2	-	5.2
National insurance and other contributions	4	32.8	-	32.8	-	32.8
Gross trading surplus	5	-0.5	0.7	0.2	7.6	7.9
Rent and miscellaneous current transfers	6	0.4	2.8	3.2	0.5	3.8
Interest and dividends from private sector and abroad	7	3.4	1.2	4.6	0.7	5.2
Interest and dividends within public sector	8	6.0	-4.0	2.0	-2.0	-
Imputed charge for non-trading capital consumption	9	1.3	1.6	2.9	-	2.9
Capital transfers from private sector	10	-	-	-	0.2	0.2
Total receipts	**11**	**169.4**	**21.2**	**190.5**	**6.7**	**197.3**
Current and capital expenditure						
Current expenditure on goods and services	12	56.8	36.4	93.2	-	93.2
Subsidies	13	4.0	1.0	4.9	-	4.9
Current grants to personal sector	14	49.2	5.0	54.2	-	54.2
Current grants paid abroad	15	2.9	-	2.9	-	2.9
Current grants within public sector	16	24.0	-23.9	-	-	-
Debt Interest	17	17.6	0.6	18.2	0.6	18.8
Gross domestic fixed capital formation	18	4.0	2.9	6.9	5.0	11.9
Increase in stocks	19	-0.3	-	-0.3	0.3	0.1
Capital grants to private sector	20	3.1	0.6	3.6	0.1	3.7
Capital grants within public sector	21	1.8	-1.0	0.8	-0.8	-
Total expenditure	**22**	**163.0**	**21.5**	**184.5**	**5.2**	**189.8**
Unallocated Reserve	23	-	-	-	-	-
Financial surplus	**24**	**6.3**	**-0.4**	**6.0**	**1.5**	**7.5**
Financial transactions						
Net lending to private sector and abroad	25	0.5	-0.3	0.3	-	0.3
Cash expenditure on company securities (including privatisation proceeds)	26	-7.1	0.1	-7.0	-	-7.1
Transactions concerning certain public sector pension schemes	27	-0.7	-	-0.7	-	-0.7
Accruals adjustments	28	-0.1	-0.2	-0.4	-	-0.3
Miscellaneous financial transactions	29	0.1	0.7	1.3	0.6	1.4
Debt repayment	**30**	**13.7**	**-0.6**	**13.1**	**1.0**	**14.0**

1 Financial surplus (line 24) = receipts (line 11) - expenditure (line 22) - Reserve (line 23).
Debt repayment (line 30) = financial surplus (line 24) - financial transactions (lines 25 to 29).

2. Including community charge in Scotland

Please check all signs carefully

£ billion
1989-90 Forecast

Line	General government: Central government	General government: Local authorities	General government: Total	Public corporations	Public sector	
						Current and capital receipts
1	69.2	-	69.2	-0.6	68.5	Taxes on income, and oil royalties
2	60.8	20.4	81.2	-	81.2	Taxes on expenditure and community charge
3	5.3	-	5.3	-	5.3	Taxes on capital
4	34.6	-	34.6	-	34.6	National insurance and other contributions
5	-0.5	0.8	0.3	8.1	8.4	Gross trading surplus
6	0.3	3.0	3.3	0.7	4.0	Rent and miscellaneous current transfers
7	3.2	1.4	4.5	0.6	5.1	Interest and dividends from private sector and abroad
8	6.5	-4.2	2.3	-2.3	-	Interest and dividends within public sector
9	1.4	1.7	3.1	-	3.1	Imputed charge for non-trading capital consumption
10	-	-	-	0.2	0.2	Capital transfers from private sector
11	**180.8**	**23.0**	**203.8**	**6.7**	**210.5**	**Total receipts**
						Current and capital expenditure
12	61.5	37.0	98.5	-	98.5	Current expenditure on goods and services
13	4.4	0.9	5.3	-	5.4	Subsidies
14	52.9	5.8	58.8	-	58.8	Current grants to personal sector
15	4.0	-	4.0	-	4.0	Current grants paid abroad
16	24.8	-24.8	-	-	-	Current grants with public sector
17	16.2	0.4	16.6	0.5	17.1	Debt interest
18	5.0	1.9	6.9	5.6	12.5	Gross domestic fixed capital formation
19	-0.2	-	-0.1	0.2	-0.1	Increase in stocks
20	2.4	0.7	3.1	0.1	3.2	Capital grants to private sector
21	2.2	-1.1	1.1	-1.1	-	Capital grants within public sector
22	**173.3**	**21.0**	**194.3**	**5.2**	**199.5**	**Total expenditure**
23		~~22.5~~			3.5	Unallocated Reserve
24					**7.5**	**Financial surplus**
						Financial transactions
25	0.4	-0.2	0.2	-	0.2	Net lending to private sector and abroad
26	-5.0	-	-5.0	-	-5.0	Cash expenditure on company securities (including privatisation proceeds)
27	-0.3	-	-0.3	-	-0.3	Transactions concerning certain public sector pension schemes
28	-0.6	-0.2	-0.8	-	-0.8	Accruals adjustments
29	1.0	0.2	1.2	0.1	1.3	Miscellaneous financial transactions
30					**12.0**	**Debt repayment**

pso.jt/Sargent/4.27.2

BUDGET SECRET

Copy No 2 of 27 Copies

From: S D H SARGENT

Date: 27 February 1989

MR RILEY

cc Chancellor
Chief Secretary
Financial Secretary
Paymaster General
Economic Secretary
Sir T Burns
Mr Anson
Mr Wicks
Mr Scholar
Mr Culpin
Mrs Lomax
Mr Sedgwick
Mrs R Butler
Mr S Davies
Mr Gilhooly
Mr Mowl
Mr Macpherson
Miss Simpson
Miss Wallace
Mrs Chaplin
Mr Tyrie
Mr Call

PS/IR
PS/C&E

Ch
Peter wants a tougher inflation statement. Any views?

OK

AA

FSBR CHAPTER 1

Sir Peter Middleton has seen your minute of 23 February to the Chancellor. He thought that the third sentence of paragraph 1.83 looked a bit feeble on inflation for the present conjuncture. He suggests that it should be replaced by the following:

> "Monetary policy is designed to bring down money GDP growth and thus inflation over the medium term with the ultimate objective of achieving stable prices. The path for the growth of money GDP falls to around 5¼% over the next four years. Monetary policy is conducted ..."

S D H SARGENT
Private Secretary

fp.pk/macpherson/1.3.03

COPY NO 14 OF 23 COPIES

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

X below is unwelcome. It allows the industry scope to parade its own figures of longterm yeild, which may be considerably higher than the Revenue's if they choose to make a fuss about spreading acquisition expenses.

FROM: N I MACPHERSON
DATE: 1 March 1989

1. MR GILHOOLY
2. CHANCELLOR

cc: Chief Secretary
Financial Secretary
Paymaster General
Economic Secretary
Sir Peter Middleton
Sir Terence Burns
Mr Anson
Mr Scholar
Mr Culpin
Mr Riley
Mr A C S Allan
Mr Matthews
Miss Simpson
Mrs Chaplin
Mr Tyrie
Mr Call

Sir Anthony Battishill) IR
Mr Calder)

Mr Unwin) C&E
Mr P R H Allen)

BUDGET SECRET

B.L.O. SECRET

FSBR CHAPTER 4

Attached is a redraft of Chapter 4. It would be very helpful if we could have comments during the course of tomorrow.

2. Regarding the questions you raised on the last draft:

(i) the chattels exemption does apply to companies as well;

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

BUDGET SECRET B.L.O. SECRET

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

(ii) the Revenue do not feel sufficiently confident about the 'mature' yield from the life assurance package to want to publish an estimate in the FSBR. There is therefore no reference to the long-term yield in note 22 of the Annex;

(iii) there is no NIC flow back from earnings rule abolition, because no behavioural response has been assumed. The £5 million benefit flow back in the second year has been netted out of the public expenditure estimate.

3. You may want to consider the following redraft to the second age allowance indent in para. 4.02, since the current draft is unclear to some:

> "the age allowance for those aged 75 and over will rise from £3180 (for single people aged under 80) and from £3310 (for single people aged 80 and over) to £3540; and from £5035 (for married couples aged under 80) and from £5205 (for married couples aged 80 and over) to £5565."

This has the effect of putting two bits of bad news on the first page of Chapter 4. (It now follows cars).

4. I have moved relocation expenses to the first page since now that Schedule E assessment has been dropped it would have sat rather oddly between PEPs and Pensions. The Revenue want an estimate of the long term yield from abolishing the additional housing costs ESC in the Annex. I have therefore amended note 9 accordingly. However, you may not want to draw attention to this, given the high figure of £100 million.

5. I have not inserted a Pensioner's Earnings Rule side-heading by para. 4.40, since it is debatable whether a public expenditure measure should be in Chapter 4. Including it as a national insurance measure, which strictly speaking it is, allows us to get off the hook.

[initials] 1/3

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

6. The Economic Secretary has now redrafted the ECJ section and the Financial Secretary the Keith section.

Nick Macpherson

N I MACPHERSON

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

4 The Budget Tax and National Insurance Proposals in Detail

4.01 The main tax and national insurance changes proposed in the Budget are summarised below. A full list of changes is given in Table 4.1.

Income tax

4.02 The ~~main~~ income tax thresholds will be increased in line with the statutory indexation provisions (based on the increase of 6·8 per cent in the RPI in the year to December 1988); the higher level of age allowance currently ~~for~~ given to those aged 80 and over will be extended to those aged 75 and over. This will mean that:

the single person's and wife's earned income allowances will rise from £2 605 to £2 785;

the married allowance will rise from £4 095 to £4 375;

the additional personal allowance and widow's bereavement allowance will rise from £1 490 to £1 590;

the age allowance for those aged 65 to 74 will rise from £3 180 to £3 400 (single) and from £5 035 to £5 385 (married);

the age allowance for those aged 75 and over will rise from £~~3 150~~ 3180 for those under 80 and from £3 310 for those aged 80 and over to £3 540 (single), and from £5 035 for those under 80 and from £5 205 for those aged 80 and over to £5 565 (married);

the income limit for age allowance will rise from £10 600 to £11 400;

the basic rate limit will rise from £19 300 to £20 700 of taxable income.

4.03 The age allowance withdrawal rate will be reduced from £2 of allowances for each £3 of income to £1 for each £2 of income above the limit of £11 400.

Benefits in kind

4.04 Car benefit scale charges will be increased by ~~20 per cent~~ one third from 6 April 1989.

Insert old 4.12

Private medical insurance

~~4.05~~ 4.06 Income tax relief will be given from April 1990 on private medical insurance premiums for those aged 60 and over.

Charitable giving

~~4.06~~ 4.07 The limit on charitable donations qualifying for tax relief under the payroll giving scheme will be doubled from £240 to £480 a year from 6 April 1989.

Employee share ownership plans (ESOPs)

~~4.07~~ 4.08 Tax relief will be given for payments by companies to qualifying ESOP trusts.

Approved employee share schemes

~~4.08~~ 4.09 The annual limit for individual participation in the 1978 all-employee share scheme will be increased to £2 000 or—if greater—10 per cent of pay up to a maximum of £6 000. The 1980 SAYE share option~~s~~ scheme limit will be increased from £100 to £150 per month. The maximum discount from the share price at which options may be granted under these schemes will be doubled to 20 per cent.

Profit-related pay 4.10 ~~4.09~~ The cash ceiling on the amount of profit-related pay attracting tax relief will be increased to £4 000. A number of other changes will simplify and improve PRP.

Personal equity plans 4.11 ~~4.10~~ The annual limit on investment in Personal Equity Plans will be increased from £3 000 to £4 800. The annual limit on investment in unit and investment trusts will be increased to £2 400, irrespective of other holdings, and restricted to unit and investment trusts which invest mainly in UK equities. The PEP rules will be greatly simplified.

~~**Schedule E assessment**~~ ~~4.11 The basis of assessment for Schedule E (remuneration of employees and directors) will be changed from earnings to receipts. In practice, most employees are taxed on this basis already.~~

Relocation expenses 4.05 ~~4.12~~ Payments an employer makes towards the additional housing costs of an employee transferred to a more expensive location will no longer be exempt from tax.

Move to after 4.04

Pensions 4.12 ~~4.13~~ The tax regime for pensions will be amended. For occupational schemes the main features will be:

employers will be able to set up "top up" schemes for their employees, with no limits on benefits, but without special tax reliefs;

a limit will be placed on pensions paid from tax approved schemes, based on earnings of £60 000 a year. This is consistent with a privileged pension of up to £40 000 a year or maximum tax free lump sum of up to £90 000. The limit will be indexed to prices;

the rules for tax approved pensions, particularly affecting those who take early retirement, will be simplified and improved.

These changes will apply to schemes set up on or after Budget day and to new members joining existing schemes on or after that date.

4.13 ~~4.14~~ New simplified rules will be introduced for monitoring additional voluntary contributions. Any surplus contributions made will be returned to employees, subject to a special tax charge.

4.14 ~~4.15~~ Annual contribution limits for personal pension schemes will be increased as a percentage of earnings, subject to an overall cash limit based on the £60 000 earnings limit for occupational schemes.

Life assurance 4.15 ~~4.16~~ The tax regime for life assurance companies will be reformed. The main changes to be introduced from 1 January 1990 are:

pension and general annuity business expenses will be deductible only from pension or general annuity profits;

relief for expenses of acquiring new life assurance business (other than pension or general annuity business) will be spread over seven years: this change will be phased in gradually over ~~the~~ four years;

the rate of tax charged on income and capital gains attributable to policy holders will be reduced to a rate equal to the basic rate of income tax (25 per cent);

life assurance policy duty will be abolished.

Stamp Duties ~~4.17~~ 4.16 Stamp duties on share transactions will be abolished from 1 April 1990.

Unit trusts ~~4.18~~ 4.17 A new tax regime will be introduced from 1 January 1990 for unit trusts investing in transferable securities which are freely marketable throughout the European Community under the UCITS directive. The rate of corporation tax charged on their income will be reduced to a rate equal to the basic rate of income tax (25 per cent).

COBO and deep discounted bonds ~~4.19~~ 4.18 The new issues queue will be abolished by a general consent under the Control of Borrowing Order and the regime for deep discounted bonds, including certain index-linked bonds, will be amended with effect from Budget day.

Business taxation ~~4.20~~ 4.19 The profits limit for the small companies' corporation tax rate of 25 per cent for financial year 1989 will be raised from £100 000 to £150 000 and the limit for marginal relief will be raised from £500 000 to £750 000.

~~4.21~~ 4.20. The main rate of corporation tax for the financial year 1989 will be 35 per cent.

~~4.22~~ 4.21 The apportionment rules for close companies will be abolished. Special provisions including a corporation tax rate equal to the higher rate of income tax (40 per cent) will be introduced for close investment companies which distribute less than a specified percentage of their profits.

~~4.23 Unincorporated businessmen who make trading losses which can be set off against their other income will be able to set off any unused balance of their losses against capital gains.~~

Capital gains tax ~~4.24~~ 4.22 The capital gains tax annual exempt amount will remain at £5 000 in the case of individuals and £2 500 in the case of most trusts.

~~4.25~~ 4.23 The disposal value limit below which chattels are exempt from charges on capital gains will be ~~increased~~ doubled from £3 000 to ~~£5 000.~~ £6 000.

~~4.26~~ 4.24 Capital gains tax deferral on lifetime gifts will be restricted to certain types of gift—in particular, gifts of business and heritage assets, gifts on which there is an immediate charge to inheritance tax, and gifts to charity.

Inheritance tax ~~4.27~~ 4.25 From Budget day the threshold for inheritance tax will be increased in line with the statutory indexation provisions from £110 000 to £118 000.

VAT and Car Tax ~~4.28~~ 4.26 The present turnover requirements for VAT registration will be replaced for most businesses by a single limit based on turnover in the previous twelve months.

~~4.29~~ 4.27 From 15 March 1989 the VAT registration limit will be raised to £23 600 a year.

~~4.30~~ 4.28 Changes will be introduced to make relief from VAT on bad debts more widely available.

~~4.31~~ 4.29 ~~The default surcharge regime will be~~ eased by reducing the maximum rate of penalty from 30 per cent to 20 per cent.

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

4.30 ~~4.32~~ To comply with the European Court judgement of 21 June 1988 certain previously zero rated goods and services will be subject to VAT at the standard rate. As announced on 6 February, the regime will aim to minimise the tax and compliance burden.

4.31 ~~4.33~~ Non-residential construction and property development will be liable to VAT from 1 April 1989 with transitional relief for prior contractual commitments. Landlords will be given the option to tax rents of non-residential buildings from 1 August 1989. VAT will also be applied:

from 1 April 1989 to:	protective boots and helmets supplied to employers;
	news services;
from 1 July 1990 to:	fuel and power supplied to businesses;
	water and sewerage services supplied to industry.

4.32 ~~4.34~~ VAT relief for charities will be extended to charity fund-raising events, certain types of advertising and medical sterilising equipment. Cars leased to the disabled will be relieved of car tax.

Excise duty 4.33 ~~4.35~~ The duty on unleaded petrol will be reduced by the equivalent of just under 1p a litre (~~over 2p~~ nearly 4p a gallon) including VAT. A higher rate of duty will be introduced on 2 and 3 star leaded petrol. This will add ~~just over~~ nearly 1p a litre (~~5p~~ 4p a gallon) including VAT to the tax charged on these grades.

ITV levy 4.34 ~~4.36~~ From 1 January 1990, the additional payments made by ITV programme contractors will be assessed on a mixture of net advertising revenue and profits.

Tax administration 4.35 ~~4.37~~ In the light of recommendations by the Keith Committee, changes will be made:

Replace with FST redraft attached

~~to update the system of monetary penalties for tax offences;~~

~~to modernise the powers of the Inland Revenue to obtain information;~~

~~to improve compliance by employers.~~

Tax confidentiality 4.36 ~~4.38~~ Criminal sanctions will be provided against unlawful disclosure of information relating to a taxpayer by employees or former employees of the Inland Revenue and Customs and Excise.

National Insurance 4.37 ~~4.39~~ From [2] October, changes are proposed to the structure of national insurance contributions. Employees will pay Class 1 contributions equal to 2 per cent of earnings below the lower earnings limit (£43 a week in 1989–90) and 9 per cent of earnings above the lower earnings limit, up to the upper earnings limit (£325 a week in 1989–90). Those earning below the lower earnings limit will continue to pay no Class 1 contributions.

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

4.40 From [2] October the rule whereby state retirement pensioners earning more than £75 a week have their pensions reduced, and those earning over £120 a week have their pension abated entirely, will be abolished. The public expenditure cost of abolition will be about £125 million in 1989–90 and £255 million in 1990–91. This cost will be met from the Reserve, and is therefore not included in Table 4.1. (Nor does Table 4.1 include the increased tax revenue that will flow from the changes, £25 million in 1989–90 and £65 million in 1990–91.)

4.41 These changes to national insurance contributions and the pensioners' earnings rule will be included in the Social Security Bill now before Parliament.

4.38 The flat rate Class 2 contributions paid by the self employed will be reduced from £4.25 a week to £2.95 a week from October 1989.

4.39 The Class 3 voluntary contributions will be reduced from £4.15 to £2.85 a week from October 1989.

BUDGET SECRET
BUDGET LIST ONLY
NOT TO BE COPIED

Table 4.1 Direct effects of changes in taxation and national insurance

See Annex 4 Paragraph numbers	£ million Estimated effect on receipts in: 1989–90 Changes from a non-indexed base	1989–90 Changes from an indexed base	1990–91 Changes from an indexed base
INLAND REVENUE			
Income tax			
1 Increase in single allowance of £180 and married allowance of £280	−1 130	—	—
2 Increase in additional personal allowance and widow's bereavement allowance of £100	−10	—	—
3 Increase in age allowances in line with statutory indexation	−100	—	—
4 Extend higher age allowances for those aged 80 and over to those aged 75 and over	−10	−10	−15
5 Increase in income limit for age allowance of £800	−15	—	—
6 Reduction in age allowance withdrawal rate	−5	−5	−5
7 Increase in basic rate limit of £1 400 to £20 700	−210	—	—
8 Fringe benefits—~~20 per cent~~ one third increase in car benefit scales	~~+90~~ +160	~~+90~~ +160	~~+110~~ +200
9 Removal of extra-statutory concession on additional housing costs	+5	+5	+30
10 Tax relief for private medical insurance for those aged 60 or over	—	—	−40
11 Pension schemes—amendments to tax rules	*	*	*
12 Payroll giving to charities—increase in donation limit to £480 a year	*	*	*
13 Membership covenants to heritage charities	−5	−5	−10
14 Liberalisation of profit-related pay legislation	−10	−10	−15
15 Increase in approved employee share limits	*	*	*
16 Employee priority in public offer of shares	*	*	*
17 Changes in material interest tests	*	*	−5
18 Abolition of tax relief on new loans to buy Business Expansion Scheme shares	*	*	+5
~~19 Schedule E—change to receipts basis of assessment~~	~~−60~~	~~−60~~	~~−80~~
20 Changes in settlements provisions where settlor or spouse can benefit	*	*	*
21 Tax deductible from tax credit payments to US companies	—	—	—
Income tax and corporation tax			
22 Taxation of income, gains and profits of life assurance companies	*	*	+125
23 Abolition of close company apportionment	*	*	*
24 Capital allowances—safety at sports grounds and miscellaneous amendments	*	*	*
25 Extension of relief for pre-trading expenditure	*	*	*
26 Subcontractor tax scheme—reduction in ~~voucher~~ paperwork requirements	—	—	—
Income tax and capital gains tax			
27 Personal Equity Plans—increase in limits etc.	−5	−5	−10
~~28 Unincorporated businesses—set off of trading losses against gains~~	~~*~~	~~*~~	~~*~~
Income tax, corporation tax and capital gains tax			
29 Keith committee—administrative changes	*	*	*
30 Deep discounted bonds—taxation of uplift as income	—	—	+15
31 Tax charge on switching investments in offshore funds	*	*	*
Corporation tax			
32 Increase in profits limits for small companies rate and marginal relief	*	*	−35
33 Reduction in tax rate for certain unit trusts	—	—	*
34 Relief for payments to ESOP trusts	*	*	*
35 Advance corporation tax amendments	*	*	*
Thin → 36 Sale of subsidiaries	*	*	*
Capital gains tax			
37 No change in annual exempt amount	—	*	+10
38 Restriction of gifts relief	*	*	+25
39 Change in the rules for Lloyd's underwriters	—	—	*

* = *Negligible* — = *Nil*

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

Table 4.1 Direct effects of changes in taxation—*continued*

See Annex 4 paragraph numbers	£ million Estimated effect on receipts in: 1989–90 Changes from a non-indexed base	1989–90 Changes from an indexed base	1990–91 Changes from an indexed base
Capital gains tax and corporation tax			
40 UK branches of foreign businesses—changes affecting capital gains	*	*	*
41 Technical changes associated with rebasing of capital gains	*	*	*
42 Increase in capital gains chattels exemption to £5 000	*	*	*
43 Exemption of certain bonds from charges on capital gains	*	*	*
Capital gains tax and inheritance tax			
44 Gifts to housing associations	*	*	*
Inheritance tax			
45 Increase of £8 000 in threshold	−35	—	—
46 Changes in rules for varying dispositions on death	+5	+5	+15
Stamp duties			
47 Abolition of duties on shares	+10	+10	−1 000
48 Abolition of life assurance policy duty	−20	−20	−80
TOTAL INLAND REVENUE	~~−1 505~~ −1375	~~−5~~ +125	~~−985~~ −790
CUSTOMS AND EXCISE			
Value added tax			
49 Revised registration rules	−35	−35	−100
50 Increase in registration limit	*	*	*
51 Bad debt relief	−50	−50	−150
52 Keith—review of default surcharge	−20	−20	−20
~~**53** Recovery of overpaid VAT and excise duty~~	~~—~~	~~—~~	~~—~~
54 Revised tax regime for construction, buildings and land	+310	+310	+440
55 Change in liability of news services	+5	+5	+5
56 Change in liability of certain protective boots and helmets	*	*	*
57 Change in liability of certain supplies of fuel and power	—	—	+95
58 Change in liability of certain water and sewerage services	—	—	*
59 Reliefs for charities	−5	−5	−5
60 Relief for research and development cars	~~−5~~ *	~~−5~~ *	−5
Car tax			
61 Relief for vehicles leased to disabled	~~−5~~ −10	~~−5~~ −10	−10
Excise duties			
62 No change in rate of spirits duty	—	−65	−70
63 No change in rate of beer duty	—	−140	−155
64 No change in rate of duty on cider and perry	—	−5	−5
65 No change in rate of duty on wine and made-wine	—	−45	−50
66 No change in rate of duty on 4 star petrol etc.	—	−440	−465
67 No change in rate of duty on derv	—	−95	−105
68 No change in rate of duty on minor oils	—	−10	−10
69 No change in rates of tobacco products duties	—	−235	−250
70 Restriction on blending of duty-paid made-wine	*	*	*
71 Determination of original gravity of beer	*	*	*
72 Reduction in duty on unleaded petrol	~~−30~~ ~~[illegible]~~ −35	~~−30~~ −35	~~−60~~ −90
73 Increase in duty on 2 star and 3 star petrol	~~*~~ −5	~~*~~ −5	~~−15~~ −10
TOTAL CUSTOMS AND EXCISE	~~+165~~ +155	~~−870~~ −880	~~−935~~ −960
Vehicle excise duty			
74 No change in VED on cars, light vans and main lorry rates	—	−190	−210
75 Increase in VED rates for taxis, buses and coaches	+20	+20	+20
76 Increase in certain other VED rates	+20	+20	+20
TOTAL VED	**+40**	**−150**	**−170**

* = *Negligible* — = *Nil*

Table 4.1 Direct effects of changes in taxation—*continued*

See Annex 4 paragraph numbers	£ million Estimated effect on receipts in: 1989–90 Changes from a non-indexed base	 Changes from an indexed base	 1990–91 Changes from an indexed base
Other			
77 ITV levy re-basing	—	—	+50
78 Unauthorised disclosure of confidential information	—	—	—
TOTAL OTHER	—	—	+50
TOTAL CHANGES IN TAXATION	~~−1300~~ −1180	~~−1025~~ −905	~~−2040~~ −1870
National insurance contributions			
79 Restructure employee contributions	−985	−985	−2785
TOTAL CHANGES TO NATIONAL INSURANCE CONTRIBUTIONS	−1020 ~~−985~~	−1020 ~~−985~~	−2935 ~~−2785~~
80 Reduce Class 2 contributions	−35	~~−145~~ −35	−145
81 Reduce Class 3 contributions	*	*	−5

* = *Negligible* — = *Nil*

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

4.35 In light of recommendations by the Keith Committee, measures are proposed to

- simplify and update the system of interest and monetary penalties for tax offences;

- modernise the Inland Revenue's powers for information about a taxpayer under enquiry to allow questions to be put to the taxpayer and provide greater safeguards for him or her;

- amend the Inland Revenue's search powers to provide greater protection for him or her;

- improve compliance by employers in filing end of year returns of PAYE and NIC deductions.

Annex to Chapter 4

Explanatory notes to Table 4.1

Table 4.1 gives the direct effects of changes in taxation. Estimates are rounded to the nearest £5 million. "Negligible" means less than £3 million.

The direct effect of a tax change is the difference between the yield of the tax which would arise on the basis of the rate of tax, allowances, etc prevailing before the Budget (the pre-Budget regime) and the yield after the changes proposed in the Budget (the post-Budget regime). The difference in yield is generally calculated by applying the pre- and post-Budget regimes to the same tax base. This base is the post-Budget base—that is, the levels of income, consumption, profits, etc forecast for future years on the assumption that all the measures proposed in the Budget take effect.

Tax changes may cause changes in taxpayers' behaviour, which in turn can alter the tax base and hence revenue. The direct effects are estimated subject to the constraint that, in general, total incomes and total expenditure are fixed at their post-Budget levels. Thus the estimates in the table do not include income effects—that is, effects arising solely from the impact of changes in taxes on disposable incomes. Nor do they include the effects of changes in the tax base arising from changes in pre-tax incomes, the general level of prices or other macro-economic variables which may result from the proposed tax change. But other behavioural effects are taken into account where it is thought that they will have a significant effect on the yield.

For Customs and Excise taxes and duties, all the estimates of yield incorporate the effects of the tax changes on relative prices and associated changes in the pattern of consumers' expenditure. Aggregate income and consumers' expenditure at factor cost are assumed not to change. This is a slight modification of previous practice in which nominal consumers' expenditure at market prices, rather than at factor cost, was held constant. Examples where behavioural effects are taken into account for Inland Revenue taxes include the abolition of stamp duties on share transactions and changes involving the take-up of a new or modified relief.

The post-Budget forecast of each tax given in Table 1.2 takes account of all the effects of the measures announced in the Budget, and not just the direct effects included in Table 4.1.

The figures in the first column of Table 4.1 show the direct effect of the Budget proposals on receipts in 1989–90. Budget proposals are compared with a non-indexed base—that is, with the pre-Budget regime of allowances, thresholds and rates of duty at 1988–89 levels.

The figures in the second column show the direct effect of the Budget proposals on receipts in 1989–90, measured against an indexed base. The indexed base for 1989–90 is obtained by increasing 1988–89 allowances, thresholds and rates of duty by 6·8 per cent, the increase in the RPI over the year to December 1988.

The figures in the third column show the direct effect on receipts in 1990-91, also measured against an indexed base. For this comparison, both the Budget proposals and the indexed base for 1989–90 have been further indexed by the forecast movement in the RPI between the fourth quarters of 1988 and 1989 (shown in Table 3.12).

The remainder of this annex provides a commentary on the Budget proposals in Table 4.1; the paragraph numbers refer to the lines in this table. Additional information is provided for those proposals where the effect on tax liabilities in the first complete year to which the change applies (full year effect) is substantially different from the effect on receipts in either 1989–90 or 1990–91; or where the impact of the proposal is expected to build up over a period of years.

Income Tax

1 to **5** The increases in the ~~main personal~~ income tax allowances are in line with the statutory indexation provisions (based on the increase of 6·8 per cent in the RPI in the year to December 1988). The higher age allowance currently given to those aged 80 and over will be extended to those aged 75 ~~years~~ and over. The cost of indexation for those aged between 75 and 79 is included in line 3.

6 The age allowance withdrawal rate will be reduced from £2 of allowances for each £3 of income to £1 for each £2 of income above the limit of £11 400.

7 The increase in the basic rate limit is in line with the statutory indexation provisions.

8 For 1989–90 the scales for taxing car benefits will be increased by ~~20 per cent~~ one third from their 1988–89 levels.

9 The extra-statutory concession which has exempted from tax certain reimbursements by employers of additional housing costs incurred by their employees who have had to move with their jobs to more expensive locations will be withdrawn from 6 April 1989, subject to transitional arrangements. A statutory relief will be introduced to replace the extra-statutory concession which has exempted ~~certain job-related removal expenses from any charge to income tax.~~

employees from tax on the cost of removal expenses paid by employers. Tax yield of these measures will be of the order of £100 million after transitional arrangements have ceased to take effect.

10 Tax relief will be available (with basic rate relief given at source) for eligible premiums paid in 1990–91 and subsequent years for private medical insurance for those aged 60 years and over. The cost for 1990–91 assumes an increase in take-up in the region of 10 per cent as a result of the new relief. Eventual costs will depend, among other things, on the extent to which medical insurance for the over-60s is promoted and taken up.

11 The amendments to the tax rules for pension schemes will mean that:

for tax approved schemes, earnings over £60 000 will be ignored for the purpose of calculating benefits (consistent with a maximum pension of £40 000, or tax-free lump sum of £90 000). Other amendments will be made to the tax rules to improve early retirement benefits, to allow a two-thirds final salary pension on retirement after 20 years' service between ages 50 and 70 and to simplify calculation of tax-free lump sums. These changes apply to new schemes set up on or after 14 March 1989 and to new members joining existing schemes on or after that date;

employers will be able to set up top-up schemes with no limits on benefits, but without tax privileges such as tax-free investment build-up;

new rules will allow surplus voluntary contributions to be returned to the member instead of reducing benefits from the employer's scheme. The voluntary scheme will deduct a 35 per cent charge from the refund to recoup the tax advantages enjoyed on contributions and build-up. There will be a further liability on higher rate taxpayers;

changes will be made to the personal pensions tax rules to increase from 1988–89 the age related contribution limits. The increased limit will be subject to the £60 000 earnings cap. And the rules for calculating tax-free lump sums will be simplified.

These measures are expected to have a broadly neutral revenue effect in the early years.

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

12 The limit on charitable donations qualifying for relief under payroll deduction schemes will be increased from £240 to £480 from April 1989. The cost will depend on take-up.

13 The conditions for relief for charitable covenants will be relaxed so that where a member of a heritage charity is given free entry to view the charity's property, that benefit will not disqualify the covenant payments from relief. The cost will depend on take-up.

14 Amendments to the profit related pay (PRP) legislation will:

abolish the "5 per cent test" on a PRP scheme's eligibility for registration;

increase to £4 000 the cash limit on the amount of PRP attracting tax relief;

allow scheme employers to alter, subject to conditions, the rules of PRP schemes already registered; and

enable PRP schemes to be registered for certain employment units using the profits of the whole business rather than of the employment unit itself.

15 The annual limit on the value of shares which may be given to an employee under an approved all-employee profit-sharing share scheme will be increased, with effect from 6 April 1989, from £1 250 (or 10 per cent of pay up to a maximum of £5 000) to £2 000 (or 10 per cent of pay up to £6 000). The limit on monthly savings made by an employee under an approved savings-related share option scheme will be increased, from a day to be appointed, from £100 to £150. The maximum discount on the share price at which options may be granted under these schemes will be increased from 10 per cent to 20 per cent. The use of consortium shares in an approved employee share scheme will be extended to any member of a consortium owning 5 per cent or more of the company's ordinary share capital in place of the previous 15 per cent limit.

16 There will be relaxations in the conditions under which income tax relief is given to employees who benefit by virtue of their employment from priority in applying for a public offer of shares.

17 Changes will be made in the material interest tests relating to an employee's eligibility to participate in an approved employee share scheme or a registered profit-related pay scheme, and an individual's entitlement to close company interest relief. Subject to certain conditions, shares held by a trust of which the employee is a beneficiary will be disregarded when reckoning whether he has material interest.

18 Relief for interest on loans to acquire Business Expansion Scheme shares on or after 14 March 1989 will be abolished.

19 From 6 April 1989 Schedule E emoluments will ~~be assessed~~ for the year in which they are received instead of the year for which they are earned. There will be a transitional cost, ~~but from~~ 1992–93 when the transition is complete, there will be ~~an annual~~ yield of about £50 million.

20 A change will be made to the provisions which treat certain settlement income as the settlor's for higher rate tax purposes to ensure that income from outright gifts between husband and wife will be treated under Independent Taxation as the income of the recipient of the gift. For certain other settlements the present rule will be extended to the basic rate producing a small revenue yield.

21 Legislation will be introduced to make clear the amount of UK tax that is deductible from UK tax credits to which non-residents may be entitled under a double taxation convention. This measure will prevent a potential Exchequer loss of about £15 million a year.

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

Income tax and corporation tax

22 From 1 January 1990, the rules for taxing life assurance companies will be changed:

to allow relief for the expenses of pension, general annuity and other life assurance business only against their respective profits;

to spread the relief for the costs of acquiring new business (other than pension and general annuity business) over seven years, subject to transitional arrangements in the first four years to phase out the present immediate relief; and

to reduce the corporation tax rate on income and capital gains ~~allowable~~ attributable to policyholders to 25 per cent.

The yield in 1990–91 and the immediately following years is reduced by the proposed transitional arrangements, and by the carry-forward of unrelieved expenses from past years. The yield in all years depends on developments in the industry, particularly in the level of new business, and is therefore highly uncertain.

23 The apportionment rules for close companies will be abolished. A higher rate of corporation tax equal to the higher rate of income tax of 40 per cent will be introduced for close investment companies which distribute less than a specified percentage of their profits. A close investment company will no longer get tax relief for interest payments, annual payments or management expenses unless these would have been deductible if paid by an individual.

24 The legislation relating to capital allowances for safety expenditure at sports grounds will be amended from 1 January 1989 to take account of the extension of safety certificate requirements to regulated stands at undesignated sports grounds. Minor amendments will be made to the capital allowances legislation to correct defects and anomalies in advance of the consolidation of that legislation.

25 The period for which relief may be available for business expenditure incurred before a trade begins will be increased from three to five years. The cost of this proposal will take some years to build up and could amount of tens of millions of pounds.

26 Subject to consultation, the paperwork requirements of the scheme for subcontractors in the construction industry will be reduced. ~~for example by aggregation of small payments onto a single voucher.~~

Income tax and capital gains tax

27 The main changes are:

an increase in the overall annual limit on investment in a Personal Equity Plan to £4 800;

within that an increase in the limit for investment in authorised unit trusts and investment trusts to £2 400, coupled with a new requirement that the trust must invest mostly in UK equities;

significant simplifications for plan managers; and

the facility for new share issues to be brought within plans.

The costs assume take-up in the region of 400 000 in the first full year. The cost is likely to reach £30 million after five years.

~~**28** After 5 April 1989, if an unincorporated trader makes a loss which can be set off against other income of the same and/or the following year, he will be able to set any unused loss against his capital gains. The estimated full year costs accrued in 1989–90 and 1990–91 are £50 million and £75 million respectively.~~

Income tax, corporation tax and capital gains tax

29 In the light of recommendations of the Keith Committee, administrative changes will be made:

to update the system of monetary penalties for tax offences in line with inflation and remove obsolete penalties;

~~to introduce a uniform time limit of 20 years for recovery of tax lost through default;~~

to allow taxpayers further time to claim reliefs where an Inspector discovers that further tax is due;

to modernise the Inland Revenue's powers to obtain information about a taxpayer under enquiry, to allow questions to be put to the taxpayer, provide greater safeguards for the taxpayer and protect audit papers and tax advice from disclosure by his accountant;

to amend the Inland Revenue's search powers to provide greater safeguards for the taxpayer;

to create a new criminal offence for the deliberate destruction of documents called for under the Inland Revenue's information powers;

to change the filing date for returns of PAYE and NIC deductions by employers from 19 April to 19 May, tighten up the penalties for late filing gradually over a period of years, leading to the introduction of automatic penalties for all late filing (but not before 1995).

The effect on revenue in subsequent years is expected to be small.

30 From Budget day the existing corporate deep discount legislation in Schedule 4 ICTA 1988 will be widened to include non-variable deep discounted securities issued by non-corporate borrowers. On a sale or redemption the accrued discount will be taxed as income. Any excess or shortfall will be taxed as a capital gain or loss unless the security is exempt from capital gains tax as a qualifying corporate bond. Where deep discounted securities have variable features so that the precise accrued discount at any particular time cannot be determined in advance (including certain index linked bonds), the whole of the uplift between cost price and sale or redemption price will be taxed as income. The eventual yield is uncertain but is estimated at around £50 million.

31 A tax charge will be imposed on UK investors on gains when they switch holdings within an offshore fund.

Corporation Tax

32 The profits limit for the small companies' corporation tax rate of 25 per cent for financial year 1989 will be raised from £100 000 to £150 000 and the limit for marginal relief will be raised from £500 000 to £750 000.

33 From 1 January 1990 all unit trusts that are UCITS (Undertakings for Collective Investment in Transferable Securities) under the relevant European Communities legislation will be subject to corporation tax on their income at a rate of 25 per cent. The cost will rise to about £20 million from 1991–92 onwards.

34 Payments made by a company to an ESOP trust will be deductible in calculating its corporation tax liability where the trust meets conditions aimed at ensuring the distribution ~~acquisition~~ of shares in the company to all of ~~by~~ its employees, on similar terms, within a reasonable time.

35 Various minor changes will be made to the advance corporation tax (ACT) rules concerning a company which is part of a group or consortium.

36 Measures will be introduced to counter avoidance of tax on disposals of subsidiaries in ways which could cause a substantial loss of tax.

Capital Gains Tax

37 The capital gains tax annual exempt amount will remain at £5 000 in the case of individuals and £2500 in the case of most trusts.

38 Capital gains tax gifts relief (which allows deferral on gifts) will be restricted to certain types of gift, the main categories being gifts of business and heritage assets and gifts on which there is an immediate charge to inheritance tax. The revenue yield in 1991-92 is estimated at £40 million. The change will not affect gifts to charities or between spouses.

39 The capital gains tax rules and rules about the transfer of securities applying to assets held by Lloyd's underwriters in their premiums trust funds will be amended to facilitate stock lending to market makers.

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

Capital Gains Tax and Corporation Tax

40 Changes will be made to the rules for the taxation of capital gains of foreign businesses with UK branches or agencies or with operations on the UK continental shelf. The main effect will be to counter possible developments which could lead to a significant loss of tax.

41 Technical changes will be made in relation to the application of the provisions in the Finance Act 1988 for rebasing the taxation of capital gains to 1982 in certain special situations.

42 Chattels with a disposal value of less than £3 000 are exempt from charges on capital gains. The limit will be ~~raised~~ doubled to £6 000.

43 Certain sterling bonds will be exempted from capital gains tax and corporation tax on gains. The main effect will be to counter use of the indexation allowance in ways which could cause a significant loss of tax.

Capital gains tax and Inheritance Tax

44 ~~Certain~~ Gifts of land to registered housing associations will qualify for capital gains tax deferral and inheritance tax exemption.

Inheritance Tax

45 The estimated full year cost of indexation attributable to taxable estates in 1989–90 is £80 million.

46 The facility for varying the disposition of a deceased person's assets will be limited to those variations making adequate provision for his or her dependants.

Stamp Duty

47 The following stamp duties will be abolished from 1 April 1990:

the ½ per cent *ad valorem* duty on the transfer of UK registered securities;

stamp duty reserve tax;

the 1½ per cent duties on the conversion of UK shares into depository receipts or their transfer into clearance services;

associated charges on bearer shares and unit trusts units; and

certain fixed duties on share transfers.

Announcement of the abolition of these duties is expected to lead to some rise in the value of share transactions. That will mean an increased yield from stamp duty and value added tax in 1989–90 and from some other taxes, eg capital gains tax in later years. The figures in Table 4.1 take account of these additional yields.

Technical changes will ensure that, in the period up to 1 April 1990, any paperless share deals bear stamp duties on the same basis as paper-based transactions.

48 Life assurance policy duty will be abolished from 1 January 1990. The cost in 1990–91 takes account of the consequential change in corporation tax liability.

Value Added Tax

49 The present VAT registration rules will be replaced by a single requirement based on turnover in the previous twelve months. The existing rules based on anticipated turnover will still apply, in modified form, to large businesses and short term events.

50 From 15 March 1989, the registration limit will become £23 600 a year.

51 A comprehensive system of VAT relief on all debts which are more than 18 months old and which have been written off in the trader's accounts will be introduced. Repayment of the relief, or part of it, will be required where the debt is subsequently paid in whole or in part.

52 The maximum rate of default surcharge will be reduced from 30 per cent to 20 per cent for all appropriate VAT returns due on or after 31 March 1989.

53 The right of taxpayers to recover overpaid VAT, excise duty [and car tax] will be confirmed—subject to certain conditions—and procedures established which will enable VAT accounting errors to be corrected.

54 From 1 April 1989, VAT will be applied at the standard rate to the construction and sale of new non-residential buildings. From 1 August 1989, landlords will be able to opt to charge tax on their non-residential property and land transactions and VAT at the standard rate will be applied, in ~~certain~~ limited circumstances, to building land where this is necessary to ensure fair competition.

where the tenant is a charity

Tenants whose landlords opt to tax existing leases will pay tax on only half of the rent in the first year. ~~In the case of charities~~ The phasing in period will be five years. Transitional relief will allow zero rating to continue for certain developments where legal commitments had been entered into before 21 June 1988.

55 From 1 April 1989, VAT will be applied at the standard rate to news services (but not newspapers).

56 From 1 April 1989, VAT will be applied at the standard rate to protective boots and helmets supplied to employers.

57 From 1 July 1990, VAT will be applied at the standard rate to fuel and power supplied to businesses.

58 From 1 July 1990, VAT will be applied at the standard rate to water and sewerage services supplied to industry.

59 From 1 April 1989, VAT relief for charities will be extended to charity and certain other fund-raising events, medical sterilising equipment and classified and certain other types of advertising.

60 From 1 ~~May~~ August 1989, all cars used by manufacturers for research and development purposes will be relieved of VAT.

Car Tax

61 From ~~Royal Assent~~ 1 April, vehicles leased to the disabled will be relieved of car tax.

Excise duties

62–69 There will be no change in the rates of duty on alcoholic drinks, tobacco products and most hydrocarbon oils.

70 The duty arrangements for made-wine will be brought into line with those applicable to wine (of fresh grapes) by prohibiting duty-paid blending.

71 The rules for determining the original gravity of beer for duty purposes will be clarified.

72 The duty on unleaded petrol will be reduced by the equivalent of ~~0.7~~ 0.8p a litre (~~3.2~~ 3.6p a gallon) including VAT.

73 A higher rate of duty will be introduced on two and three star leaded petrol. This will add ~~1.1~~ 1.0p a litre (~~5p~~ 4.4p a gallon) including VAT to the tax charged on these grades. ~~Cost of extra take-up of unleaded petrol exceeds yield from two star in 1990–91.~~ Despite the increase in duty, the revenue effect of this change is negative as a result of expected switching from 2 star to unleaded petrol.

Vehicle excise duties

74 There will be no change in the duties on cars, light vans, motor cycles and most lorries.

75 From 15 March 1989, the number of duty rates for taxis, coaches and lorries will be reduced from over sixty to five and rates will be adjusted.

76 From 15 March 1989, the rates of duty on certain rigid lorries will be increased to bring them more into line with rates for articulated vehicles of similar gross weight. The rate of duty for special types capable of carrying very long, wide or heavy loads will be increased to £3 100.

Other

77 From 1 January 1990, the additional payments made by ITV programme contractors will be assessed on a mixture of net advertising revenue and profits.

78 Criminal sanctions will be provided against unlawful disclosure of information relating to ~~an identifiable~~ a taxpayer by employees or former employees ~~of revenue departments.~~ of the Inland Revenue and Customs and Excise.

National Insurance Contributions

79 From 2 October 1989, employees will pay Class 1 contributions equal to 2 per cent of earnings below the lower earnings limit (£43 a week in 1989–90) and 9 per cent of earnings above the lower earnings limit, up to the upper earnings limit (£325 a week in 1989–90). Those earning below the lower earnings limit will continue to pay no Class 1 contributions.

80 From 2 October 1989, flat rate Class 2 contributions paid by the self employed will be reduced from £4 25 a week to £2 45 a week.

81 From 2 October 1989, Class 3 voluntary contributions will be reduced from £4 15 a week to £2 35 a week.

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

fp.pk/macpherson/1.3.03

COPY NO 1 OF 23 COPIES

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

BUDGET SECRET

X below is unwelcome. It allows the industry scope to parade its own figures of longterm yield, which may be considerably higher than the Revenue's if they choose to make a fuss about spreading acquisition expenses.

FROM: N I MACPHERSON
DATE: 1 March 1989

1. MR GILHOOLY

2. CHANCELLOR

cc: Chief Secretary
Financial Secretary
Paymaster General
Economic Secretary
Sir Peter Middleton
Sir Terence Burns
Mr Anson
Mr Scholar
Mr Culpin
Mr Riley
Mr A C S Allan
Mr Matthews
Miss Simpson
Mrs Chaplin
Mr Tyrie
Mr Call

Sir Anthony Battishill) IR
Mr Calder)

Mr Unwin) C&E
Mr P R H Allen)

a OK? A few comments.

Re X, yes, noted.
2. A few other small points, passim.

SECRET

B.L.O.

FSBR CHAPTER 4

Attached is a redraft of Chapter 4. It would be very helpful if we could have comments during the course of tomorrow.

2. Regarding the questions you raised on the last draft:

(i) the chattels exemption does apply to companies as well;

SECRET

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

Surely they should be pressed further?

As to Culpin?

(ii) the Revenue do not feel sufficiently confident about the 'mature' yield from the life assurance package to want to publish an estimate in the FSBR. There is therefore no reference to the long-term yield in note 22 of the Annex;

(iii) there is no NIC flow back from earnings rule abolition, because no behavioural response has been assumed. The £5 million benefit flow back in the second year has been netted out of the public expenditure estimate.

3. You may want to consider the following redraft to the second age allowance indent in para. 4.02, since the current draft is unclear to some:

"the age allowance for those aged 75 and over will rise from £3180 (for single people aged under 80) and from £3310 (for single people aged 80 and over) to £3540; and from £5035 (for married couples aged under 80) and from £5205 (for married couples aged 80 and over) to £5565."

OK?

OK

4. I have moved relocation expenses to the first page since now that Schedule E assessment has been dropped may be reinstated it would have sat rather oddly between PEPs and Pensions. The Revenue want an estimate of the long term yield from abolishing the additional housing costs ESC in the Annex. I have therefore amended note 9 accordingly. However, you may not want to draw attention to this, given the high figure of £100 million. — astonishingly high.

This has the effect of putting two bits of bad news on the first page of chapter 4. (It now follows cars).

1/3

[illegible] on the [illegible]

5. I have not inserted a Pensioner's Earnings Rule side-heading by para. 4.40, since it is debatable whether a public expenditure measure should be in Chapter 4. Including it as a national insurance measure, which strictly speaking it is, allows us to get off the hook.

Neat

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

6. The Economic Secretary has now redrafted the ECJ section and the Financial Secretary the Keith section.

Nick Macpherson

N I MACPHERSON

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

4 The Budget Tax and National Insurance Proposals in Detail

4.01 The main tax and national insurance changes proposed in the Budget are summarised below. A full list of changes is given in Table 4.1.

Income tax

4.02 The ~~main~~ income tax thresholds will be increased in line with the statutory indexation provisions (based on the increase of 6·8 per cent in the RPI in the year to December 1988); the higher level of age allowance currently ~~for~~ given to those aged 80 and over will be extended to those aged 75 and over. This will mean that:

the single person's and wife's earned income allowances will rise from £2 605 to £2 785;

the married allowance will rise from £4 095 to £4 375;

the additional personal allowance and widow's bereavement allowance will rise from £1 490 to £1 590;

the age allowance for those aged 65 to 74 will rise from £3 180 to £3 400 (single) and from £5 035 to £5 385 (married);

see cover note. OK

the age allowance for those aged 75 and over will rise from ~~£3 150~~ 3180 for those under 80 and from £3 310 for those aged 80 and over to £3 540 (single), and from £5 035 for those under 80 and from £5 205 for those aged 80 and over to £5 565 (married);

the income limit for age allowance will rise from £10 600 to £11 400;

the basic rate limit will rise from £19 300 to £20 700 of taxable income.

4.03 The age allowance withdrawal rate will be reduced from £2 of allowances for each £3 of income to £1 for each £2 of income above the limit of £11 400.

Benefits in kind

4.04 Car benefit scale charges will be increased by ~~20 per cent~~ one third from 6 April 1989.

Insert old 4.12

Private medical insurance

~~4.05~~ 4.06 Income tax relief will be given from April 1990 on private medical insurance premiums for those aged 60 and over.

Charitable giving

~~4.06~~ 4.07 The limit on charitable donations qualifying for tax relief under the payroll giving scheme will be doubled from £240 to £480 a year from 6 April 1989.

Employee share ownership plans (ESOPs)

~~4.07~~ 4.08 Tax relief will be given for payments by companies to qualifying ESOP trusts.

Approved employee share schemes

~~4.08~~ 4.09 The annual limit for individual participation in the 1978 all-employee share scheme will be increased to £2 000 or—if greater—10 per cent of pay up to a maximum of £6 000. The 1980 SAYE share options scheme limit will be increased from £100 to £150 per month. The maximum discount from the share price at which options may be granted under these schemes will be doubled to 20 per cent.

0010

why?

Profit-related pay ~~4.09~~ 4.10 The cash ceiling on the amount of profit-related pay attracting tax relief will be increased to £4 000. A number of other changes will simplify and improve PRP.

Personal equity plans ~~4.10~~ 4.11 The annual limit on investment in Personal Equity Plans will be increased from £3 000 to £4 800. The annual limit on investment in unit and investment trusts will be increased to £2 400, irrespective of other holdings, and restricted to unit and investment trusts which invest mainly in UK equities. The PEP rules will be greatly simplified.

STEP?

~~**Schedule E assessment** 4.11 The basis of assessment for Schedule E (remuneration of employees and directors) will be changed from earnings to receipts. In practice, most employees are taxed on this basis already.~~ [If in, need to give reason for this measure]

Relocation expenses ~~4.12~~ 4.05 Payments an employer makes towards the additional housing costs of an employee transferred to a more expensive location will no longer be exempt from tax.

Move to after 4.04?

Pensions ~~4.13~~ 4.12 The tax regime for pensions will be amended. For occupational schemes the main features will be:

employers will be able to set up "top up" schemes for their employees, with no limits on benefits, but without special tax reliefs;

a limit will be placed on pensions paid from tax approved schemes, based on earnings of £60 000 a year. This is consistent with a privileged pension of up to £40 000 a year or maximum tax free lump sum of up to £90 000. The limit will be indexed to prices;

the rules for tax approved pensions, particularly affecting those who take early retirement, will be simplified and improved.

These changes will apply to schemes set up on or after Budget day and to new members joining existing schemes on or after that date.

~~4.14~~ 4.13 New simplified rules will be introduced for monitoring additional voluntary contributions. Any surplus contributions made will be returned to employees, subject to a special tax charge.

~~4.15~~ 4.14 Annual contribution limits for personal pension schemes will be increased as a percentage of earnings, subject to an overall cash limit based on the £60 000 earnings limit for occupational schemes.

Life assurance ~~4.16~~ 4.15 The tax regime for life assurance companies will be reformed. The main changes, to be introduced from 1 January 1990 are:

pension and general annuity business expenses will be deductible only from pension or general annuity profits;

relief for expenses of acquiring new life assurance business (other than pension or general annuity business) will be spread over seven years: this change will be phased in gradually over ~~the~~ four years;

the rate of tax charged on income and capital gains attributable to policy holders will be reduced to a rate equal to the basic rate of income tax (25 per cent);

life assurance policy duty will be abolished.

8

~~**Stamp Duties**~~ 4.16 ~~4.17 Stamp duties on share transactions will be abolished from 1 April 1990.~~

Unit trusts 4.17 ~~4.18~~ A new tax regime will be introduced from 1 January 1990 for unit trusts investing in transferable securities which are freely marketable throughout the European Community under the UCITS directive. The rate of corporation tax charged on their income will be reduced to a rate equal to the basic rate of income tax (25 per cent).

COBO and deep discounted bonds 4.18 ~~4.19~~ The new issues queue will be abolished by a general consent under the Control of Borrowing Order and the regime for deep discounted bonds, including certain index-linked bonds, will be amended with effect from Budget day.

Business taxation 4.19 ~~4.20~~ The profits limit for the small companies' corporation tax rate of 25 per cent for financial year 1989 will be raised from £100 000 to £150 000 and the limit for marginal relief will be raised from £500 000 to £750 000.

4.20 ~~4.21~~. The main rate of corporation tax for the financial year 1989 will be 35 per cent.

4.21 ~~4.22~~ The apportionment rules for close companies will be abolished. Special provisions including a corporation tax rate equal to the higher rate of income tax (40 per cent) will be introduced for close investment companies which distribute less than a specified percentage of their profits.

STET ?

~~4.23 Unincorporated businessmen who make trading losses which can be set off against their other income will be able to set off any unused balance of their losses against capital gains.~~

Capital gains tax 4.22 ~~4.24~~ The capital gains tax annual exempt amount will remain at £5 000 in the case of individuals and £2 500 in the case of most trusts.

4.23 ~~4.25~~ The disposal value limit below which chattels are exempt from charges on capital gains will be doubled ~~increased~~ from £3 000 to ~~£5 000.~~ £6 000.

4.24 ~~4.26~~ Capital gains tax deferral on lifetime gifts will be restricted to certain types of gift—in particular, gifts of business and heritage assets, gifts on which there is an immediate charge to inheritance tax, and gifts to charity.

Inheritance tax 4.25 ~~4.27~~ From Budget day the threshold for inheritance tax will be increased in line with the statutory indexation provisions from £110 000 to £118 000.

VAT and Car Tax 4.26 ~~4.28~~ The present turnover requirements for VAT registration will be replaced for most businesses by a single limit based on turnover in the previous twelve months.

4.27 ~~4.29~~ From 15 March 1989 the VAT registration limit will be raised to £23 600 a year.

4.28 ~~4.30~~ Changes will be introduced to make relief from VAT on bad debts more widely available.

4.29 ~~4.31~~ The default surcharge regime will be eased by reducing the maximum rate of penalty from 30 per cent to 20 per cent.

4.30 ~~4.32~~ To comply with the European Court judgement of 21 June 1988 certain previously zero rated goods and services will be subject to VAT at the standard rate. As announced on 6 February, the regime will aim to minimise the tax and compliance burden.

4.31 ~~4.33~~ Non-residential construction and property development will be liable to VAT from 1 April 1989 with transitional relief for prior contractual commitments. Landlords will be given the option to tax rents of non-residential buildings from 1 August 1989. VAT will also be applied~~:~~

from 1 April 1989 to~~:~~ protective boots and helmets supplied to employers; and to

news services. And from

from 1 July 1990 it will be applied to~~:~~ fuel and power supplied to businesses; and to

water and sewerage services supplied to industry.

4.32 ~~4.34~~ VAT relief for charities will be extended to charity fund-raising events, certain types of advertising and medical sterilising equipment. Cars leased to the disabled will be relieved of car tax.

Excise duty 4.33 ~~4.35~~ The duty on unleaded petrol will be reduced by the equivalent of just under 1p a litre (~~over 3p~~ nearly 4p a gallon) including VAT. A higher rate of duty will be introduced on 2 and 3 star leaded petrol. This will add ~~just over~~ nearly 1p a litre (~~5p~~ 4p a gallon) including VAT to the tax charged on these grades.

ITV levy 4.34 ~~4.36~~ From 1 January 1990, the additional payments made by ITV programme contractors will be assessed on a mixture of net advertising revenue and profits.

Tax administration 4.35 ~~4.37~~ ~~In the light of recommendations by the Keith Committee, changes will be made:~~

~~to update the system of monetary penalties for tax offences;~~

~~to modernise the powers of the Inland Revenue to obtain information;~~

~~to improve compliance by employers.~~

Replace with FST redraft attached

Tax confidentiality 4.36 ~~4.38~~ Criminal sanctions will be provided against unlawful disclosure of information relating to a taxpayer by employees or former employees of the Inland Revenue and Customs and Excise.

National Insurance 4.37 ~~4.39~~ From [1] (Monday) October, ~~changes are proposed to~~ the structure of (Employees') national insurance contributions will be reformed. Employees will pay Class 1 contributions equal to 2 per cent of earnings ~~below~~ up to the lower earnings limit (£43 a week in 1989–90) and 9 per cent of earnings above the lower earnings limit, up to the upper earnings limit (£325 a week in 1989–90). Those earning below the lower earnings limit will continue to pay no Class 1 contributions.

~~? or 'restructured'~~

new figs, 1 from

4.40 From [1] October the rule whereby state retirement pensioners earning more than £75 a week have their pensions reduced, and those earning over £120 a week have their pension abated entirely, will be abolished. The public expenditure cost of abolition will be about £125 million in 1989–90 and £255 million in 1990–91. This cost will be met from the Reserve, and is therefore not included in Table 4.1. (Nor does Table 4.1 include the increased tax revenue that will flow from the changes, estimated at £25 million in 1989–90 and £65 million in 1990–91.)

4.41 These changes to national insurance contributions and the pensioners' earnings rule will be included in the Social Security Bill now before Parliament.

~~4.38 The flat rate Class 2 contributions paid by the self employed will be reduced from £4.25 a week to £2.95 a week from October 1989.~~

4.39 The Class 3 voluntary contributions will be reduced from £4.15 to £2.85 a week from October 1989.

? do we do this if no change to Class II.

Table 4.1 Direct effects of changes in taxation and national insurance

See Annex 4 Paragraph numbers	£ million Estimated effect on receipts in: 1989–90 Changes from a non-indexed base	Changes from an indexed base	1990–91 Changes from an indexed base
INLAND REVENUE			
Income tax			
1 Increase in single allowance of £180 and married allowance of £280	−1 130	—	—
2 Increase in additional personal allowance and widow's bereavement allowance of £100	−10	—	—
3 Increase in age allowances in line with statutory indexation	−100	—	—
4 Extend higher age allowances for those aged 80 and over to those aged 75 and over	−10	−10	−15
5 Increase in income limit for age allowance of £800	−15	—	—
6 Reduction in age allowance withdrawal rate	−5	−5	−5
7 Increase in basic rate limit of £1 400 to £20 700	−210	—	—
8 Fringe benefits—~~20 per cent~~ one third increase in car benefit scales	~~+90~~ +160	~~+90~~ +160	~~+110~~ +200
9 Removal of extra-statutory concession on additional housing costs	+5	+5	+30
10 Tax relief for private medical insurance for those aged 60 or over	—	—	−40
11 Pension schemes—amendments to tax rules	*	*	*
12 Payroll giving to charities—increase in donation limit to £480 a year	*	*	*
13 Membership covenants to heritage charities	−5	−5	−10
14 Liberalisation of profit-related pay legislation	−10	−10	−15
15 Increase in approved employee share limits	*	*	*
16 Employee priority in public offer of shares	*	*	*
17 Changes in material interest tests	*	*	−5
18 Abolition of tax relief on new loans to buy Business Expansion Scheme shares	*	*	+5
~~19 Schedule E—change to receipts basis of assessment~~	~~−60~~	~~−60~~	~~−80~~
20 Changes in settlements provisions where settlor or spouse can benefit	*	*	*
21 Tax deductible from tax credit payments to US companies	—	—	—
Income tax and corporation tax			
22 Taxation of income, gains and profits of life assurance companies	*	*	+125
23 Abolition of close company apportionment	*	*	*
24 Capital allowances—safety at sports grounds and miscellaneous amendments	*	*	*
25 Extension of relief for pre-trading expenditure ?	*	*	*
26 Subcontractor tax scheme—reduction in ~~voucher~~ paperwork requirements	—	—	—
Income tax and capital gains tax			
27 Personal Equity Plans—increase in limits etc.	−5	−5	−10
~~28 Unincorporated businesses—set off of trading losses against gains~~	~~*~~	~~*~~	~~*~~
Income tax, corporation tax and capital gains tax			
29 Keith committee—administrative changes	*	*	*
30 Deep discounted bonds—taxation of uplift as income	—	—	+15
31 Tax charge on switching investments in offshore funds	*	*	*
Corporation tax			
32 Increase in profits limits for small companies rate and marginal relief	*	*	−35
33 Reduction in tax rate for certain unit trusts	—	—	*
34 Relief for payments to ESOP trusts	*	*	*
35 Advance corporation tax amendments	*	*	*
this 36 Sale of subsidiaries	*	*	*
Capital gains tax			
37 No change in annual exempt amount	—	*	+10
38 Restriction of gifts relief	*	*	+25
39 Change in the rules for Lloyd's underwriters	—	—	*

* = *Negligible* — = *Nil*

Table 4.1 Direct effects of changes in taxation—*continued*

See Annex 4 paragraph numbers	£ million Estimated effect on receipts in: 1989–90 Changes from a non-indexed base	 Changes from an indexed base	 1990–91 Changes from an indexed base
Capital gains tax and corporation tax			
40 UK branches of foreign businesses—changes affecting capital gains	*	*	*
41 Technical changes associated with rebasing of capital gains	*	*	*
42 Increase in capital gains chattels exemption to £5 000	*	*	*
43 Exemption of certain bonds from charges on capital gains	*	*	*
Capital gains tax and inheritance tax			
44 Gifts to housing associations	*	*	*
Inheritance tax			
45 Increase of £8 000 in threshold	−35	—	—
46 Changes in rules for varying dispositions on death	+5	+5	+15
Stamp duties			
47 Abolition of duties on shares	+10	+10	−1 000
48 Abolition of life assurance policy duty	−20	−20	−80
TOTAL INLAND REVENUE	~~−1 505~~ −1375	~~−5~~ +125	~~−985~~ −790
CUSTOMS AND EXCISE			
Value added tax			
49 Revised registration rules	−35	−35	−100
50 Increase in registration limit	*	*	*
51 Bad debt relief	−50	−50	−150
52 Keith—review of default surcharge	−20	−20	−20
~~**53** Recovery of overpaid VAT and excise duty~~	~~—~~	~~—~~	~~—~~
54 Revised tax regime for construction, buildings and land	+310	+310	+440
55 Change in liability of news services	+5	+5	+5
56 Change in liability of certain protective boots and helmets	*	*	*
57 Change in liability of certain supplies of fuel and power	—	—	+95
58 Change in liability of certain water and sewerage services	—	—	*
59 Reliefs for charities	−5	−5	−5
60 Relief for research and development cars	~~−5~~ *	~~−5~~ *	−5
Car tax			
61 Relief for vehicles leased to disabled	~~−5~~ −10	~~−5~~ −10	−10
Excise duties			
62 No change in rate of spirits duty	—	−65	−70
63 No change in rate of beer duty	—	−140	−155
64 No change in rate of duty on cider and perry	—	−5	−5
65 No change in rate of duty on wine and made-wine	—	−45	−50
66 No change in rate of duty on 4 star petrol etc.	—	−440	−465
67 No change in rate of duty on derv	—	−95	−105
68 No change in rate of duty on minor oils	—	−10	−10
69 No change in rates of tobacco products duties	—	−235	−250
70 Restriction on blending of duty-paid made-wine	*	*	*
71 Determination of original gravity of beer	*	*	*
72 Reduction in duty on unleaded petrol	~~−30~~ ~~−160~~ −35	~~−30~~ −35	~~−60~~ −90
73 Increase in duty on 2 star and 3 star petrol	~~*~~ −5	~~*~~ −5	~~−15~~ −10
TOTAL CUSTOMS AND EXCISE	~~+165~~ +155	~~−870~~ −880	~~−935~~ −960
Vehicle excise duty			
74 No change in VED on cars, light vans and main lorry rates	—	−190	−210
75 Increase in VED rates for taxis, buses and coaches	+20	+20	+20
76 Increase in certain other VED rates	+20	+20	+20
TOTAL VED	**+40**	**−150**	**−170**

* = *Negligible* — = *Nil*

 0016

Table 4.1 Direct effects of changes in taxation—*continued*

See Annex 4 paragraph numbers	£ million Estimated effect on receipts in: 1989–90 Changes from a non-indexed base	1989–90 Changes from an indexed base	1990–91 Changes from an indexed base
Other			
77 ITV levy re-basing	—	—	+50
78 Unauthorised disclosure of confidential information	—	—	—
TOTAL OTHER	—	—	+50
TOTAL CHANGES IN TAXATION	~~−1300~~ −1180	~~−1025~~ −905	~~−2040~~ −1870
National insurance contributions			
79 Restructure employee contributions	−985	−985	−2785
TOTAL CHANGES TO NATIONAL INSURANCE CONTRIBUTIONS	−1020 ~~−985~~	−1020 ~~−985~~	−2935 ~~−2785~~
80 Reduce Class 2 contributions	−35	~~−145~~ −35	−145
81 Reduce Class 3 contributions	*	*	−5

* = *Negligible* — = *Nil*

BUDGET SECRET—BUDGET LIST ONLY

4.35 In light of recommendations by the Keith Committee, measures are proposed to

- simplify and update the system of interest and monetary penalties for tax offences;

- modernise the Inland Revenue's powers for information about a taxpayer under enquiry to allow questions to be put to the taxpayer and provide greater safeguards ~~for him or her~~;

- amend the Inland Revenue's search powers to provide greater protection for ~~him or her~~; the taxpayer

- improve compliance by employers in filing end of year returns of PAYE and NIC deductions.

The taxpayer work

BUDGET SECRET
BUDGET LIST ONLY
NOT TO BE COPIED

Annex to Chapter 4

Explanatory notes to Table 4.1

Table 4.1 gives the direct effects of changes in taxation. Estimates are rounded to the nearest £5 million. "Negligible" means less than £3 million.

The direct effect of a tax change is the difference between the yield of the tax which would arise on the basis of the rate of tax, allowances, etc prevailing before the Budget (the pre-Budget regime) and the yield after the changes proposed in the Budget (the post-Budget regime). The difference in yield is generally calculated by applying the pre- and post-Budget regimes to the same tax base. This base is the post-Budget base—that is, the levels of income, consumption, profits, etc forecast for future years on the assumption that all the measures proposed in the Budget take effect.

Tax changes may cause changes in taxpayers' behaviour, which in turn can alter the tax base and hence revenue. The direct effects are estimated subject to the constraint that, in general, total incomes and total expenditure are fixed at their post-Budget levels. Thus the estimates in the table do not include income effects—that is, effects arising solely from the impact of changes in taxes on disposable incomes. Nor do they include the effects of changes in the tax base arising from changes in pre-tax incomes, the general level of prices or other macro-economic variables which may result from the proposed tax change. But other behavioural effects are taken into account where it is thought that they will have a significant effect on the yield.

For Customs and Excise taxes and duties, all the estimates of yield incorporate the effects of the tax changes on relative prices and associated changes in the pattern of consumers' expenditure. Aggregate income and consumers' expenditure at factor cost are assumed not to change. This is a slight modification of previous practice in which nominal consumers' expenditure at market prices, rather than at factor cost, was held constant. Examples where behavioural effects are taken into account for Inland Revenue taxes include the abolition of stamp duties on share transactions and changes involving the take-up of a new or modified relief.

The post-Budget forecast of each tax given in Table 1.2 takes account of all the effects of the measures announced in the Budget, and not just the direct effects included in Table 4.1.

The figures in the first column of Table 4.1 show the direct effect of the Budget proposals on receipts in 1989–90. Budget proposals are compared with a non-indexed base—that is, with the pre-Budget regime of allowances, thresholds and rates of duty at 1988–89 levels.

The figures in the second column show the direct effect of the Budget proposals on receipts in 1989–90, measured against an indexed base. The indexed base for 1989–90 is obtained by increasing 1988–89 allowances, thresholds and rates of duty by 6·8 per cent, the increase in the RPI over the year to December 1988.

The figures in the third column show the direct effect on receipts in 1990-91, also measured against an indexed base. For this comparison, both the Budget proposals and the indexed base for 1989–90 have been further indexed by the forecast movement in the RPI between the fourth quarters of 1988 and 1989 (shown in Table 3.12).

The remainder of this annex provides a commentary on the Budget proposals in Table 4.1; the paragraph numbers refer to the lines in this table. Additional information is provided for those proposals where the effect on tax liabilities in the first complete year to which the change applies (full year effect) is substantially different from the effect on receipts in either 1989–90 or 1990–91; or where the impact of the proposal is expected to build up over a period of years.

Income Tax

1 to 5 The increases in the ~~main personal~~ income tax allowances are in line with the statutory indexation provisions (based on the increase of 6·8 per cent in the RPI in the year to December 1988). The higher age allowance currently given to those aged 80 and over will be extended to those aged 75 ~~years~~ and over. The cost of indexation for those aged between 75 and 79 is included in line 3.

6 The age allowance withdrawal rate will be reduced from £2 of allowances for each £3 of income to £1 for each £2 of income above the limit of £11 400.

7 The increase in the basic rate limit is in line with the statutory indexation provisions.

8 For 1989–90 the scales for taxing car benefits will be increased by ~~20 per cent~~ one third from their 1988–89 levels.

9 The extra-statutory concession which has exempted from tax certain reimbursements by employers of additional housing costs incurred by their employees who have had to move with their jobs to more expensive locations will be withdrawn from 6 April 1989, subject to transitional arrangements. A statutory relief will be introduced to replace the extra-statutory concession which has exempted ~~certain job-related removal expenses from any charge to income tax.~~ employees from tax on the cost of removal expenses paid by employers. Tax yield of these measures will be of the order of £100 million after transitional arrangements have ceased to take effect.

10 Tax relief will be available (with basic rate relief given at source) for eligible premiums paid in 1990–91 and subsequent years for private medical insurance for those aged 60 years and over. The cost for 1990–91 assumes an increase in take-up in the region of 10 per cent as a result of the new relief. Eventual costs will depend, among other things, on the extent to which medical insurance for the over-60s is promoted and taken up.

11 The amendments to the tax rules for pension schemes will mean that:

for tax approved schemes, earnings over £60 000 will be ignored for the purpose of calculating benefits (consistent with a maximum pension of £40 000, or tax-free lump sum of £90 000). Other amendments will be made to the tax rules to improve early retirement benefits, to allow a two-thirds final salary pension on retirement after 20 years' service between ages 50 and 70 and to simplify calculation of tax-free lump sums. These changes apply to new schemes set up on or after 14 March 1989 and to new members joining existing schemes on or after that date;

employers will be able to set up top-up schemes with no limits on benefits, but without tax privileges such as tax-free investment build-up;

new rules will allow surplus voluntary contributions to be returned to the member instead of reducing benefits from the employer's scheme. The voluntary scheme will deduct a 35 per cent charge from the refund to recoup the tax advantages enjoyed on contributions and build-up. There will be a further liability on higher rate taxpayers;

changes will be made to the personal pensions tax rules to increase from 1988–89 the age related contribution limits. The increased limit will be subject to the £60 000 earnings cap. And the rules for calculating tax-free lump sums will be simplified.

These measures are expected to have a broadly neutral revenue effect in the early years.

12 The limit on charitable donations qualifying for relief under payroll deduction schemes will be increased from £240 to £480 from April 1989. The cost will depend on take-up.

13 The conditions for relief for charitable covenants will be relaxed so that where a member of a heritage charity is given free entry to view the charity's property, that benefit will not disqualify the covenant payments from relief. The cost will depend on take-up.

14 Amendments to the profit related pay (PRP) legislation will:

abolish the "5 per cent ~~test~~" on a PRP scheme's eligibility for registration;

increase to £4 000 the cash limit on the amount of PRP attracting tax relief;

Why

allow scheme employers to alter, subject to conditions, the rules of PRP schemes already registered; and

enable PRP schemes to be registered for certain employment units using the profits of the whole business rather than of the employment unit itself.

15 The annual limit on the value of shares which may be given to an employee under an approved all-employee profit-sharing share scheme will be increased, with effect from 6 April 1989, from £1 250 (or 10 per cent of pay up to a maximum of £5 000) to £2 000 (or 10 per cent of pay up to £6 000). The limit on monthly savings made by an employee under an approved savings-related share option scheme will be increased, from a day to be appointed, from £100 to £150. The maximum discount on the share price at which options may be granted under these schemes will be increased from 10 per cent to 20 per cent. The use of consortium shares in an approved employee share scheme will be extended to any member of a consortium owning 5 per cent or more of the company's ordinary share capital in place of the previous 15 per cent limit.

16 There will be relaxations in the conditions under which income tax relief is given to employees who benefit by virtue of their employment from priority in applying for a public offer of shares.

17 Changes will be made in the material interest tests relating to an employee's eligibility to participate in an approved employee share scheme or a registered profit-related pay scheme, and an individual's entitlement to close company interest relief. Subject to certain conditions, shares held by a trust of which the employee is a beneficiary will be disregarded when reckoning whether he has material interest.

18 Relief for interest on loans to acquire Business Expansion Scheme shares on or after 14 March 1989 will be abolished.

STET maybe

19 From 6 April 1989 Schedule E emoluments will ~~be~~ assessed for the year in which they are received instead ~~of the year~~ for which they are earned. There will be a transitional cost, ~~but from~~ 1992–93 when the transition is complete, there will be ~~an annual~~ yield of about £50 million.

20 A change will be made to the provisions which treat certain settlement income as the settlor's for higher rate tax purposes to ensure that income from outright gifts between husband and wife will be treated under Independent Taxation as the income of the recipient of the gift. For certain other settlements the present rule will be extended to the basic rate producing a small revenue yield.

21 Legislation will be introduced to make clear the amount of UK tax that is deductible from UK tax credits to which non-residents may be entitled under a double taxation convention. This measure will prevent a potential Exchequer loss of about £15 million a year.

Income tax and corporation tax

22 From 1 January 1990, the rules for taxing life assurance companies will be changed:

to allow relief for the expenses of pension, general annuity and other life assurance business only against their respective profits;

to spread the relief for the costs of acquiring new business (other than pension and general annuity business) over seven years, subject to transitional arrangements in the first four years to phase out the present immediate relief; and

to reduce the corporation tax rate on income and capital gains ~~allowable~~ attributable to policyholders to 25 per cent.

The yield in 1990–91 and the immediately following years is reduced by the proposed transitional arrangements, and by the carry-forward of unrelieved expenses from past years. The yield in all years depends on developments in the industry, particularly in the level of new business, and is therefore highly uncertain.

23 The apportionment rules for close companies will be abolished. A higher rate of corporation tax equal to the higher rate of income tax of 40 per cent will be introduced for close investment companies which distribute less than a specified percentage of their profits. A close investment company will no longer get tax relief for interest payments, annual payments or management expenses unless these would have been deductible if paid by an individual.

24 The legislation relating to capital allowances for safety expenditure at sports grounds will be amended from 1 January 1989 to take account of the extension of safety certificate requirements to regulated stands at undesignated sports grounds. Minor amendments will be made to the capital allowances legislation to correct defects and anomalies in advance of the consolidation of that legislation.

25 The period for which relief may be available for business expenditure incurred before a trade begins will be increased from three to five years. The cost of this proposal will take some years to build up and could amount of tens of millions of pounds.

26 Subject to consultation, the paperwork requirements of the scheme for subcontractors in the construction industry will be reduced. ~~for example by aggregation of small payments onto a single voucher.~~

Income tax and capital gains tax

27 The main changes are:

an increase in the overall annual limit on investment in a Personal Equity Plan to £4 800;

within that an increase in the limit for investment in authorised unit trusts and investment trusts to £2 400, coupled with a new requirement that the trust must invest mostly in UK equities;

significant simplifications for plan managers; and

the facility for new share issues to be brought within plans.

The costs assume take-up in the region of 400 000 in the first full year. The cost is likely to reach £30 million after five years.

STET maybe.

28 After 5 April 1989, if an unincorporated trader makes a loss which can be set off against other income of the same and/or the following year, he will be able to set any unused loss against his capital gains. The estimated full year costs accrued in 1989–90 and 1990–91 are £50 million and £75 million respectively.

Income tax, corporation tax and capital gains tax

29 In the light of recommendations of the Keith Committee, administrative changes will be made:

to update the system of monetary penalties for tax offences in line with inflation and remove obsolete penalties;

to introduce a uniform time limit of 20 years for recovery of tax lost through default;

to allow taxpayers further time to claim reliefs where an Inspector discovers that further tax is due;

to modernise the Inland Revenue's powers to obtain information about a taxpayer under enquiry, to allow questions to be put to the taxpayer, provide greater safeguards for the taxpayer and protect audit papers and tax advice from disclosure by his accountant;

to amend the Inland Revenue's search powers to provide greater safeguards for the taxpayer;

to create a new criminal offence for the deliberate destruction of documents called for under the Inland Revenue's information powers;

to change the filing date for returns of PAYE and NIC deductions by employers from 19 April to 19 May, tighten up the penalties for late filing gradually over a period of years, leading to the introduction of automatic penalties for all late filing (but not before 1995).

The effect on revenue in subsequent years is expected to be small.

30 From Budget day the existing corporate deep discount legislation in Schedule 4 ICTA 1988 will be widened to include non-variable deep discounted securities issued by non-corporate borrowers. On a sale or redemption the accrued discount will be taxed as income. Any excess or shortfall will be taxed as a capital gain or loss unless the security is exempt from capital gains tax as a qualifying corporate bond. Where deep discounted securities have variable features so that the precise accrued discount at any particular time cannot be determined in advance (including certain index linked bonds), the whole of the uplift between cost price and sale or redemption price will be taxed as income. The eventual yield is uncertain but is estimated at around £50 million.

31 A tax charge will be imposed on UK investors on gains when they switch holdings within an offshore fund.

Corporation Tax

32 The profits limit for the small companies' corporation tax rate of 25 per cent for financial year 1989 will be raised from £100 000 to £150 000 and the limit for marginal relief will be raised from £500 000 to £750 000.

33 From 1 January 1990 all unit trusts that are UCITS (Undertakings for Collective Investment in Transferable Securities) under the relevant European Communities legislation will be subject to corporation tax on their income at a rate of 25 per cent. The cost will rise to about £20 million from 1991–92 onwards.

34 Payments made by a company to an ESOP trust will be deductible in calculating its corporation tax liability where the trust meets conditions aimed at ensuring the distribution ~~acquisition~~ of shares in the company to all of ~~by~~ its employees, on similar terms, and within a reasonable time.

35 Various minor changes will be made to the advance corporation tax (ACT) rules concerning a company which is part of a group or consortium.

36 Measures will be introduced to counter avoidance of tax on disposals of subsidiaries in ways which could cause a substantial loss of tax.

Capital Gains Tax

37 The capital gains tax annual exempt amount will remain at £5 000 in the case of individuals and £2500 in the case of most trusts.

38 Capital gains tax gifts relief (which allows deferral on gifts) will be restricted to certain types of gift, the main categories being gifts of business and heritage assets and gifts on which there is an immediate charge to inheritance tax. The revenue yield in 1991-92 is estimated at £40 million. The change will not affect gifts to charities or between spouses.

39 The capital gains tax rules and rules about the transfer of securities applying to assets held by Lloyd's underwriters in their premiums trust funds will be amended to facilitate stock lending to market makers.

Capital Gains Tax and Corporation Tax

40 Changes will be made to the rules for the taxation of capital gains of foreign businesses with UK branches or agencies or with operations on the UK continental shelf. The main effect will be to counter possible developments which could lead to a significant loss of tax.

41 Technical changes will be made in relation to the application of the provisions in the Finance Act 1988 for rebasing the taxation of capital gains to 1982 in certain special situations.

42 Chattels with a disposal value of less than £3 000 are exempt from charges on capital gains. The limit will be ~~raised~~ doubled to £6 000.

43 Certain sterling bonds will be exempted from capital gains tax and corporation tax on gains. The main effect will be to counter use of the indexation allowance in ways which could cause a significant loss of tax.

Capital gains tax and Inheritance Tax

44 ~~Certain~~ Gifts of land to registered housing associations will qualify for capital gains tax deferral and inheritance tax exemption.

Inheritance Tax

45 The estimated full year cost of indexation attributable to taxable estates in 1989–90 is £80 million.

46 The facility for varying the disposition of a deceased person's assets will be limited to those variations making adequate provision for his or her dependants.

Stamp Duty

47 The following stamp duties will be abolished from 1 April 1990:

the $\frac{1}{2}$ per cent *ad valorem* duty on the transfer of UK registered securities;

stamp duty reserve tax;

the $1\frac{1}{2}$ per cent duties on the conversion of UK shares into depository receipts or their transfer into clearance services;

associated charges on bearer shares and unit trusts units; and

certain fixed duties on share transfers.

Announcement of the abolition of these duties is expected to lead to some rise in the value of share transactions. That will mean an increased yield from stamp duty and value added tax in 1989–90 and from some other taxes, eg capital gains tax in later years. The figures in Table 4.1 take account of these additional yields.

Technical changes will ensure that, in the period up to 1 April 1990, any paperless share deals bear stamp duties on the same basis as paper-based transactions.

48 Life assurance policy duty will be abolished from 1 January 1990. The cost in 1990–91 takes account of the consequential change in corporation tax liability.

Value Added Tax

49 The present VAT registration rules will be replaced by a single requirement based on turnover in the previous twelve months. The existing rules based on anticipated turnover will still apply, in modified form, to large businesses and short term events.

50 From 15 March 1989, the registration limit will become £23 600 a year.

51 A comprehensive system of VAT relief on all debts which are more than 18 months old and which have been written off in the trader's accounts will be introduced. Repayment of the relief, or part of it, will be required where the debt is subsequently paid in whole or in part.

52 The maximum rate of default surcharge will be reduced from 30 per cent to 20 per cent for all appropriate VAT returns due on or after 31 March 1989.

53 The right of taxpayers to recover overpaid VAT, excise duty [and car tax] will be confirmed—subject to certain conditions—and procedures established which will enable VAT accounting errors to be corrected.

54 From 1 April 1989, VAT will be applied at the standard rate to the construction and sale of new non-residential buildings. From 1 August 1989, landlords will be able to opt to charge tax on their non-residential property and land transactions and VAT at the standard rate will be applied, in ~~certain~~ limited circumstances, to building land where this is necessary to ensure fair competition.

Tenants whose landlords opt to tax existing leases will pay tax on only half of the rent in the first year. ~~In the case of charities~~ The phasing in period will be five years where the tenant is a charity. Transitional relief will allow zero rating to continue for certain developments where legal commitments had been entered into before 21 June 1988.

55 From 1 April 1989, VAT will be applied at the standard rate to news services (but not newspapers).

56 From 1 April 1989, VAT will be applied at the standard rate to protective boots and helmets supplied to employers.

57 From 1 July 1990, VAT will be applied at the standard rate to fuel and power supplied to businesses.

58 From 1 July 1990, VAT will be applied at the standard rate to water and sewerage services supplied to industry.

59 From 1 April 1989, VAT relief for charities will be extended to charity and certain other fund-raising events, medical sterilising equipment and classified and certain other types of advertising.

60 From 1 ~~May~~ August 1989, all cars used by manufacturers for research and development purposes will be relieved of VAT.

Car Tax

61 From ~~Royal Assent~~ 1 April, vehicles leased to the disabled will be relieved of car tax.

Excise duties

62–69 There will be no change in the rates of duty on alcoholic drinks, tobacco products and most hydrocarbon oils.

70 The duty arrangements for made-wine will be brought into line with those applicable to wine (of fresh grapes) by prohibiting duty-paid blending.

71 The rules for determining the original gravity of beer for duty purposes will be clarified.

72 The duty on unleaded petrol will be reduced by the equivalent of ~~0·7p~~ 0.8p a litre (~~3·2p~~ 3.6p a gallon) including VAT.

73 A higher rate of duty will be introduced on two and three star leaded petrol. This will add ~~1·1p~~ 0.9p a litre (~~5p~~ 4.1p a gallon) including VAT to the tax charged on these grades. ~~Cost of extra take-up of unleaded petrol exceeds yield from two star in 1990–91.~~ Despite the increase in duty, the revenue effect of this change is negative as a result of expected switching from 2 star to unleaded petrol.

Vehicle excise duties

74 There will be no change in the duties on cars, light vans, motor cycles and most lorries.

75 From 15 March 1989, the number of duty rates for taxis, coaches and lorries will be reduced from over sixty to five and rates will be adjusted.

76 From 15 March 1989, the rates of duty on certain rigid lorries will be increased to bring them more into line with rates for articulated vehicles of similar gross weight. The rate of duty for special types capable of carrying very long, wide or heavy loads will be increased to £3 100.

Other

77 From 1 January 1990, the additional payments made by ITV programme contractors will be assessed on a mixture of net advertising revenue and profits.

78 Criminal sanctions will be provided against unlawful disclosure of information relating to ~~an identifiable~~ a taxpayer by employees or former employees ~~of revenue departments.~~ of the Inland Revenue and Customs and Excise.

National Insurance Contributions

79 From ~~1~~ 2 October 1989, employees will pay Class 1 contributions equal to 2 per cent of earnings below the lower earnings limit (£43 a week in 1989–90) and 9 per cent of earnings above the lower earnings limit, up to the upper earnings limit (£325 a week in 1989–90). Those earning below the lower earnings limit will continue to pay no Class 1 contributions.

~~80 From 2 October 1989, the rate Class 2 contributions paid by the self employed will be reduced from £4.25 a week to £2.95 a week.~~

81 From 2 October 1989, Class 3 voluntary contributions will be reduced from £4.15 a week to £2.85 a week.

FROM: S J DAVIES
DATE: 1st March 1989

COPY NO. 1 OF 29

CHANCELLOR

cc Chief Secretary
Financial Secretary
Paymaster General
Economic Secretary
Sir P Middleton
Sir T Burns
Mr Anson
Mr Wicks
Mr Monck
Mr Scholar
Mrs Lomax
Mr Peretz
Mr Riley
Mr Sedgwick
Mr Gieve
Mr Grice
Mr MacAuslan
Mr Mowl
Mr Pickford
Mr Barrie
Mr Savage
Miss J C Simpson
Mr Wallace
Mr Call
Mrs Chaplin
Mr Tyrie

[w Table 2]

MTFS FISCAL PROJECTIONS

This submission sets out provisional fiscal projections for the MTFS period. It shows projections of government revenue - after allowing for the effects of the Budget as in Mr Culpin's revised scorecard of 24 February - and projections of government expenditure. It then sets out projections of the fiscal adjustment for two alternative PSDR paths. Finally it considers presentational issues that these projections raise.

A. General government receipts

2. Table 1 shows our projections of revenues before any fiscal adjustment but after allowing for the Budget package in the latest scorecard. They are consistent with a constant underlying tax burden after 1989-90, ie with a tax burden that would be constant

if the effects of the 1988 and 1989 Budgets were taken out of the figures. These projections are extremely provisional: recent costings from the revenue departments have, in fact, been pointing to rather lower tax receipts than assumed in this submission. There is a risk of quite substantial further changes to the projections by the end of this week.

Table 1: General government receipts

£ billion, cash

	1987-88	1988-89	1989-90	1990-91	1991-92	1992-93
Taxes on incomes, expenditure and capital	133.2	144.8	156.3	163.5	172.0	181.2
National insurance and other contributions	25.0	32.8	34.5	35.8	37.8	39.9
Interest and dividends	6.1	6.8	6.9	6.7	6.3	5.6
Other receipts	5.7	6.5	6.7	6.2	6.5	7.0
General government receipts	173.5	190.9	204.4	212.2	222.6	233.8
Of which North Sea tax	4.7	3.2	2.7	2.4	2.7	2.6

3. The build up of the effects of the 1988 and 1989 Budgets causes a reduction in the tax burden over the period to 1991-92 (see table 2). The introduction of independent taxation is now estimated to be worth about ¼ percentage point off the tax burden by 1991-92. The build up of the 1989 Budget package accounts for a ½ point reduction in the tax burden between 1989-90 and 1990-91.

Table 2: Non-oil tax burden before post 1989 fiscal adjustments

	1987-88	1988-89	1989-90	1990-91	1991-92	1992-93
Projected	37.7	37.5	37.6	37.0	36.7	36.7
Before 1988 and 1989 Budget changes	37.7	38.4	39.2	39.2	39.2	39.2

4. The flat "Budget-adjusted" or "underlying" tax burden after 1989-90 shown in the second row of table 2 appears at variance with our estimate that real fiscal drag normally tends to add about 0.2 percentage points a year to the tax burden. The projections allow for a large fall in the effective tax rate on corporate profits, the result primarily of the build up of capital allowances following the 1984 corporate tax reform against the background of little growth in ICCs profits. The latest detailed set of tax projections that we have from Inland Revenue shows capital allowances used by non-oil ICCs and financial companies rising from about £16 billion in 1987 (affecting tax payments in 1988-89) to over £30 billion in 1991 (affecting tax payments in 1992-93). This on its own would account for a 0.5 percentage point <u>fall</u> in the total non-oil tax burden between 1988-89 and 1992-93, and offsets the positive real fiscal drag arising in other parts of the tax system.

5. It goes without saying that the corporation tax projections are extremely uncertain. Even if we knew past and future aggregate profits and investment with certainty there would still be a substantial margin of error around the projections, and the scope for error is greatly increased by the problems with the national accounts data for 1987 and 1988. Other things being equal, the projections for tax payments would obviously be higher if we used the published data for the recent level of investment rather than our own higher estimates.

B. General government expenditure

6. Table 3 shows our central projections of general government expenditure, given the MTFS assumptions on output, inflation etc. The public expenditure planning total is projected about

£1½ billion above the level in the public expenditure White Paper in 1990-91, and more than £3 billion above the White Paper level in 1991-92.

7. Gross debt interest payments are projected lower than in the White Paper for 1990-91 and 1991-92 despite a higher than expected estimated outturn in 1988-89: the projections for the future have been revised down because the debt interest path in the White Paper was constructed on the basis of a zero PSDR after 1989-90 and hence a higher stock of debt than is now projected. (The debt interest figures shown in table 3 have been derived on the assumption of a PSDR of £8 billion in 1990-91, £6 billion in 1991-92, and £4 billion in 1992-93.)

8. The overshoot of debt interest in 1988-89, despite a higher debt repayment, was mirrored in higher debt interest receipts. Higher interest rates and the increase in the foreign exchange reserves contributed to both higher payments and higher receipts. The path of net debt interest is shown below, together with an approximate estimate of the contribution of debt repayment, given the interest rates we are projecting.

£ billion

	1987-88	1988-89	1989-90	1990-91	1991-92	1992-93
Net debt interest	11.6	11.5	10.0	8.5	7.7	7.5
Approximate contribution of PSDR	-0	-1	-2½	-3	-3½	-4
Cumulative PSDR	-3	-17	-29	-37	-43	-47

It appears that the cumulative repayment of debt may explain about three quarters of the projected decline in net debt interest between 1988-89 and 1992-93. The other contributors are an assumed relative fall in UK interest rates, and a decline in the inflation uplift on index-linked gilts.

Table 3: General government expenditure

£ billion, cash

	1987-88	1988-89	1989-90	1990-91	1991-92	1992-93
Public expenditure planning total	145.7	150.6	167.2	180.9	195.0	205.7
Gross debt interest	17.7	18.3	17.0	15.2	14.0	13.1
Other adjustments	8.3	9.9	9.8	9.5	8.6	8.5
General government expenditure	**171.8**	**178.8**	**194.1**	**205.7**	**217.5**	**227.3**
Privatisation proceeds	-5.2	-7.0	-5.0	-5.0	-5.0	-5.0
General government expenditure excluding privatisation proceeds	**177.0**	**185.8**	**199.1**	**210.7**	**222.5**	**232.3**
GGE excluding privatisation proceeds (per cent of GDP)	41.6	39.4	39.2	39.1	39.0	38.6
		472	508	539	571	602

9. The projected levels of general government expenditure are slightly above the path published in the Autumn Statement, while the projected ratios of GGE to money GDP for 1989-90 onwards are the same as in in the Autumn Statement.

2½ 1¾ 1 ½/¼

Table 4: Comparison of paths for GGE excluding privatisation proceeds

	1988-89	1989-90	1990-91	1991-92	1992-93
£ billion					
Projections as in table 3	185.8	199.1	210.7	222.5	232.3
White Paper*	186.9	198.7	210.0	221.0	
per cent of GDP					
Projections as in table 3	39.4	39.2	39.1	39.0	38.6
White Paper	39¾	39¼	39	38¾	

* rounded for 1990-91 onwards

C. PSDR and fiscal adjustment paths

10. Bringing together the fiscal projections considered in sections A and B, table 5 shows our central estimate of the fiscal adjustment available in 1990 and later years for two different assumptions about the path of the PSDR. (We have not shown a case with a PSDR path starting with more than £8 billion in 1990-91, because of the initial increase in taxes that such a path would imply.)

Table 5: Alternative paths for the PSDR

	1989-90	1990-91	1991-92	1992-93
Case 1				
PSDR (£ billion)	12	8	6	4
PSDR (% of GDP)	2½	1½	1	¾
Annual fiscal adjustment (£ billion)		0	-1	3
Cumulative fiscal adjustment (£ billion)		0	-1	2
Non oil tax burden after fiscal adjustment (per cent)	37.6	37.1	37.0	36.1
Case 2				
PSDR (£ billion)	12	8	4	0
PSDR (% of GDP)	2½	1½	¾	0
Annual fiscal adjustment (£ billion)		0	1	5
Cumulative fiscal adjustment (£ billion)		0	1	6
Non oil tax burden after fiscal adjustment (per cent)	37.6	37.1	36.6	35.4

11. These projections suggest that a large fall in the PSDR will be required over the next two year if any further tax reductions are to be made in the 1990 and 1991 Budgets. This is because of

the build up of the effects of the 1988 and 1989 Budgets (especially in 1990-91), the growing importance of capital allowances discussed earlier, and two years of below trend growth in output*.

D. Presentational issues

(i) Expenditure

12. The expenditure figures published in the MTFS - which will, of course, be rounded - will include the public expenditure White Paper planning total path up to 1991-92. The normal convention is to stay with the planning total figures shown in the PEWP, but to allow changes in economic assumptions to come through in debt interest and "other adjustments". (In practice, however, figures for <u>total</u> GGE have not differed materially from those shown in the PEWP, at least in the last 2 years). Our current projections point to a lower debt interest path than shown in the White Paper, which assumed a £10 billion PSDR in 1988-89 and 1989-90 and zero PSDR thereafter. By contrast, the path of "other adjustments" that GEP are proposing for publication in the FSBR involves upward revisions since the White Paper. If we adopted the PEWP planning total and the current central projections for debt interest, we would end up showing GGE at virtually the same level as in the PEWP in 1989-90 and 1990-91, but £1 billion below the PEWP path in 1991-92.

13. As usual, GEP are anxious not to show any change from the figures for the planning total shown in the PEWP. This year, however, the 1989 Survey will be held on the basis of the new planning total, and this means that the main benchmark will have to be the GGE figures (both for departments and for outside commentators). The cash figures for GGE in the FSBR will therefore be of more than normal significance. The lower are the

---

* Our standard ready reckoner of the effects of variations in economic growth on the PSDR would suggest a reduction in the PSDR of 0.2 per cent of GDP in 1989-90, a further reduction of 0.3 per cent of GDP in 1990-91, and a further 0.1 per cent in 1991-92, as a result of the period of below trend growth in output.

figures published in the FSBR the more demanding the starting point against which the outcome of the Survey will be judged at the time of the 1989 Autumn Statement. And a reduction now in the figures for GGE might suggest to Departments that there was extra room within the total for programme increases. It would therefore be helpful to retain the PEWP GGE cash figures.

14. We can achieve this by relatively minor changes to the debt interest figures: the largest change would be for 1991-92 where we would need to raise debt interest by about £1 billion compared with our central projection. The scope for changing the debt interest projections is, of course, constrained by the requirement that the published path should be defensible in relation to the projection of the PSDR; but even with this adjustment to the 1991-92 debt interest figure we would be showing almost a £4 billion fall in debt interest payments between 1988-89 and 1991-92 compared with just over a £2 billion fall in the PEWP. Commentators would probably think we had taken adequate account of the prospective repayment of debt.

Gross debt interest payments **£billion**

	1988-89	1989-90	1990-91	1991-92
PEWP	17.7	17	16	15.5
Path now needed to achieve PEWP GGE numbers	18.3	16.5	15	14.5

15. Assuming we do keep the rounded PEWP numbers for GGE, we will continue to show a declining ratio of GGE excluding privatisation proceeds to GDP, with (for 1989-90 through to 1991-92) ratios at the same level as in the PEWP.

16. For 1992-93, it has been agreed that the MTFS will show 1 per cent growth in real GGE; our central projection is for more like 2 per cent real GGE growth. The consequence of showing just 1 per cent real growth in GGE will be to increase the projected

annual fiscal adjustment in 1992-93 by some £2 billion (to £5 billion in case 1 and £6 billion in case 2), unless we make some offsetting adjustments to the projections of revenue.

17. In the MTFS table which sets out the details of expenditure (table 2.3 in the most recent draft), we propose to show figures for the old planning total and "other adjustments" for 1992-93, even though figures on this basis will not be promulgated again. There is an argument for not doing so, but, on balance, it seems better not to arouse unnecessary suspicions by departing from normal practice at this stage. Table 6 shows the figures for expenditure that might appear in the MTFS. (Following the convention adopted in the 1988 Autumn Statement, debt interest and other adjustments are rounded to the nearest £0.5 billion, not, as previously, to the nearest £1 billion.)

Table 6: General government expenditure (rounded as for MTFS table 2.3)

	1987-88	**1988-89**	**1989-90**	**1990-91**	**1991-92**	**1992-93**
Public expenditure planning total	145.7	150.6	167	179	192	200
Gross debt interest	17.7	18.3	16.5	15	14.5	14
Other adjustments	8.3	9.9	10	10.5	9.5	9.5
General government expenditure	**171.8**	**178.8**	**194**	**205**	**216**	**223**
Privatisation proceeds	-5.2	-7.0	-5	-5	-5	-5
General government expenditure excluding privatisation proceeds	**177.0**	**185.8**	**199**	**210**	**221**	**228**
(Memo: ratio of GGE ex pp to GDP)	41½	39½	39¼	39	38¾	38

(ii) Tax and the fiscal adjustment

18. The two sets of PSDR/fiscal adjustment profiles shown earlier indicate that it is difficult to obtain a reasonably stylised PSDR path which yields a smooth series for the fiscal adjustment. Both the PSDR options shown in table 5 show low or negative fiscal adjustments in 1990-91 and 1991-92, followed by a large positive figure in 1992-93. This is largely unavoidable given the build up of Budget effects on taxes; and it would be consistent with what we say in the latest draft of the MTFS about the cycle and the PSDR* to have a bigger fall in the PSDR in 1990-91 and 1991-92 than in 1992-93.

19. We do of course have some latitude to change the tax projections to increase the cumulative fiscal adjustment over the whole period, and/or to smooth out the yearly pattern. But we have to be careful: there is some merit on tactical/public expenditure grounds for relatively low fiscal adjustments in the next year or so; and it would be risky to pretend that the last two Budgets had not pre-empted some of the fiscal adjustment which would otherwise have been available over the next years or so. And if we now set too ambitious a target for the 1990-91 PSDR and the projections in this note turn out to be correct, we could at the time of the 1990 Budget face the choice of either raising taxes or reducing the PSDR compared with the path established in the 1989 MTFS.

20. The net effect of the presentational adjustments to expenditure - which will involve publishing <u>lower</u> GGE figures than our central projections - together with some smoothing of taxes might get us to a publishable fiscal adjustment path using the "Case 2" PSDR path as considered earlier.

---

* "The PSDR will tend to be increased by GDP growth above trend, and to be reduced by below trend GDP growth."

Possible annual fiscal adjustment path for publication

(£billion)

	1990-91	1991-92	1992-93
PSDR Case 2	1	1	4

21. To obtain this path of the fiscal adjustment we would have to adjust our forecast path of revenues by some £½ to £¾ billion in 1990-91 and 1991-92 and make a rather larger downward adjustment to revenue growth (around £3½ billion) in the final year. Rather larger adjustments would be needed to obtain a publishable fiscal adjustment path if the "Case 1" PSDR path were adopted and this is probably not very attractive.

E. Decisions

22. The main decisions to be taken are:

- what PSDR path to adopt

- the extent to which we should smooth our projections of revenues to even out the path of the fiscal adjustment, and possibly increase the cumulative fiscal adjustment over the whole MTFS period

- should we aim to show cash GGE figures up to 1991-92 unchanged from the White Paper

SJD

S J DAVIES

rjb/485

BUDGET SECRET

COPY 1 OF 17 COPIES

FROM: MRS R J BUTLER
DATE: 1 March 1989

CHANCELLOR OF THE EXCHEQUER

m Chx. I would read the chapter.

cc PS/CST
PS/FST
PS/PMG
PS/EST
Sir P Middleton
Sir T Burns
Mr Anson
Mr Scholar
Mr Culpin
Mr Riley
Mr Sedgwick
Mrs Lomax
Mr S Davies
Miss Simpson

1989 FSBR: CHAPTER 5

I attach a copy of the amended proofs of Chapter 5 of the FSBR which takes on board the comments made by you and the Chief Secretary last week.

2. A paragraph on Budget measures (5.04) has been added and the figures for 1988-89 have been amended to take out the £483 million Electricity Council tax payment which is not now expected this year. The text of paragraph 5.06 has been modified accordingly. However, the figures for 1988-89 estimated outturn for the planning total are still being updated and will be cleared with the Chief Secretary early next week. The figures for GGE, GDP and the GDP deflator have also yet to be settled. The final figures will be incorporated next week.

3. The proofs have to be returned to the printers on Friday so I would be grateful for any further comments you may have by noon tomorrow.

RJ Butler

MRS R J BUTLER

5 Public expenditure

Anson

5.01. The Government's expenditure plans for the next three years were set out in the 1988 Autumn Statement (HC 695) and in detail in the 1989 public expenditure White Paper (Cm 601–621). They are summarised in Table 5.1. ~~The Budget makes no change to these plans.~~

Changes since previous Budget

5.02. The planning total for 1989–90 remains unchanged from the level shown in the last FSBR; the planning total for 1990–91 has been increased by £3·3 billion. In both years, extra resources have been provided to meet the Government's priorities, including substantial additional sums for health, law and order, defence and roads. Provision for local authority current spending and the UK's net contribution to the European Communities is also higher.

Table 5.1 Public expenditure

	£ billion				
	1987–88 Outturn	1988–89 Estimated outturn	1989–90 Plans	1990–91 Plans	1991–92 Plans
Department					
Social ~~S~~ecurity l.c	46·3	47·4	51·0	55·3	58·7
Health	19·7	21·8	23·2	24·4	25·4
Defence	18·9	19·0	20·1	21·2	22·1
Education and science	17·1	18·4	19·6	20·2	20·8
Home Office and legal departments	6·5	7·2	8·0	8·4	8·6
Transport	4·6	4·8	5·4	5·5	5·7
Scotland	8·1	8·7	9·0	9·1	9·7
Wales	3·3	3·6	3·8	3·9	4·0
Northern Ireland	4·9	5·6	5·5	5·7	5·9
Other departments	21·4	21·~~7~~ 2	23·1	23·7	25·2
Privatisation proceeds	−5·1	−7·0	−5·0	−5·0	−5·0
Reserve			3·5	7·0	10·5
Public expenditure planning total	**145·7**	~~**151·1**~~ 150·6	**167·1**	**179·4**	**191·6**
General government gross debt interest[1]	17·7	18·3	16·5	15~~½~~	~~15~~ 14 ½
Other adjustments[1]	8·3	9·~~4~~ 9	9·~~4~~ 9	~~9½~~ 10 ½	9 ½
General government expenditure	**171·7**	**178·8**	**193·~~0~~** 5	**205**	**216**
General government expenditure excluding privatisation proceeds:					
in real terms (base year 1987–88)[2]	177·0	173·6	178·1	181·9	185·8
as a percentage of GDP[2]	**41¾**	**39** ½	**39** ¼	~~**38¾**~~ 39	**38~~¾~~** 2

[1] *1990–91 and 1991–92 figures rounded to nearest £½ billion.*

[2] *Using GDP deflator and money GDP on the same basis as in Table 2.1.*

BUDGET SECRET—~~BUDGET LIST ONLY~~

Public spending trends

5.03. General government spending, excluding privatisation proceeds, has fallen from 46¾ per cent of GDP in 1982–83 to [39] per cent in 1988–89. The expenditure plans to 1991–92 are consistent with the Government's policy of reducing the share of national income taken by total government spending. The move to Budget surplus has reduced the burden of debt interest, and the fall in unemployment has made savings possible in the social security, employment and training programmes. These savings, together with higher housing receipts and reduced agricultural market support have made room for increases in priority programmes within the declining trend of total expenditure relative to national income.

Budget consequences

Anson

(£ 190 million in 1989-90)

5.04. The public expenditure cost of abolishing the earnings rule for state retirement pensioners will be charged to the Reserve, and will not add to planning totals. The public expenditure cost of extending VAT to non-residential construction and property development was incorporated in the plans set out in the 1988 public expenditure White Paper.

1988–89 outturn

5.05. The latest estimates for the outturn for the planning total in 1988–89, which are still subject to some uncertainty, suggest that it is likely to be £[151·1] billion, £[5·8] billion below the plans shown in the 1988 public expenditure White Paper and the 1988 Budget (of which £2 billion represents increased privatisation proceeds) and £[2·3] billion below the outturn figure shown in the 1989 public expenditure White Paper. A breakdown is shown in Table 5.2.

Table 5.2 Comparison of plans and estimated outturn for 1988–89

	1988–89 £ billion		
	Plans[1]	Estimated outturn	Outturn minus plans
Central government[2]	114·3	114·3	
Local authority[2]	42·6	42·9	+0·3
of which:			
relevant expenditure	33·2	34·5	+1·2
other current	5·4	5·3	−0·1
capital	4·0	3·1	−0·9
Nationalised industries and other public corporations	1·4	0·~~5~~ 4	~~−0·5~~ −1·0
Privatisation proceeds	−5·0	−7·0	−2·0
Reserve	3·5		−3·5
Public expenditure planning total	**156·9**	~~**151·1**~~ 150·6	~~**−5·8**~~ −6·3

[1] *Plans from The Government's Expenditure Plans 1988–89 to 1990–91 (Cm 288), adjusted for classification changes.*

[2] *Excluding finance for nationalised industries and other public corporations.*

BUDGET SECRET—~~BUDGET LIST ONLY~~ ABS 1/3

£0·9 billion additional spending on the NHS as a result of the nurses & other pay settlements,

The electricity supply industry,

latest information on tax payments by ~~electricity~~ (£0·5 billion),

5.06. The major changes in 1988–89 between programme plans in the 1988 White Paper and the estimated outturn are:

central government: increases arising from NHS pay settlements (£0·9 billion), a capital grant of £0·4 billion associated with the sale of Rover to BAe, and finance for the recapitalisation of Shorts Brothers prior to privatisation (£0·4 billion), are offset by reductions in social security expenditure (£1·0 billion) due mainly to the fall in unemployment; lower payments by the Intervention Board for Agricultural Produce (£0·4 billion) and lower expenditure on employment programmes (£0·4 billion);

local authorities: an overspend of £1·2 billion on planned current expenditure and a net underspend of £0·9 billion on capital expenditure, reflecting higher gross spending (£1·2 billion) offset by higher receipts (£2·1 billion);

nationalised industries and other public corporations: an ~~improvement~~ underspend of £~~0·5~~ 1·0 billion mainly reflecting higher profitability of British Steel prior to privatisation (£0·3 billion) and British Rail (£0·3 billion).

Table 5.3 Public expenditure by spending authority

£ billion	1987–88 Outturn	1988–89 Estimated outturn	1989–90 Plans	1990–91 Plans	1991–92 Plans
Central government[1]	109·4	114·3	123·7	131·2	136·9
of which:					
Voted in Estimates	76·9	80·7	86·9	92·2	96·4
other	32·5	33·5	36·8	39·0	40·5
Local authorities[1]	40·7	42·9	44·0	45·5	47·1
of which:					
relevant expenditure	32·0	34·5	35·2	36·5	37·5
other current	5·1	5·3	6·2	6·7	7·1
capital	3·6	3·1	2·6	2·4	2·5
Nationalised industries	0·3	0·~~1~~0	—	−0·4	1·0[2]
Other public corporations	0·5	0·5	0·9	1·0	1·1
Privatisation proceeds	−5·1	−7·0	−5·0	−5·0	−5·0
Reserve			3·5	7·0	10·5
Public expenditure planning total	**145·7**	~~**151·1**~~ 150·6	**167·1**	**179·4**	**191·6**

[1] *Excluding finance for nationalised industries and other public corporations.*

[2] *The increase in 1991–92 refleacts the disappearance from the public expenditure figures, following privatisation, of the substantial negative external finance of the electricity industry.*

Public expenditure by spending authority

5.07. Central government spending makes up about three quarters of the planning total. About 70 per cent of this is voted by Parliament through the annual Supply Estimates and covers the expenditure of government departments for their own activities as well as their funding of other bodies such as the National Health Service. Most of the remainder consists of social security payments paid out of the National Insurance Fund. Spending by local authorities accounts for about one quarter of public expenditure. Nationalised industries and other public corporations account for the remainder of the total. Table 5.3 gives outturn figures for the last two years and the plans as published in the public expenditure White Paper.

Supply Estimates **5.08**. For 1989–90, the plans set out in the public expenditure White Paper have now been translated, where appropriate, into detailed control totals in Supply Estimates. The total Estimates provision for 1989–90 for which the Government is seeking Parliamentary approval is shown in Table 5.4. The main Estimates for 1989–90 are published in a series of booklets on 14 March 1989 with a Summary and Guide (Cm ~~[ ]~~ 633) which summarises the Estimates and explains how they relate to the public expenditure planning total. It also describes the Supply procedure.

5.09. Of the £[116·0] billion included in the Supply Estimates, £[90·2] billion is direct public expenditure. The remaining £[25·8] billion does not feature directly as public expenditure because it consists of grants to local authorities and finance for other bodies whose spending is counted as public expenditure. About two thirds of the money voted in Estimates is subject to cash limits, which provide the Government with greater control over its cash expenditure during the financial year.

Table 5.4 Supply expenditure

	£ billion			
	1987–88		1988–89	1989–90
	Expected outturn in 1987 Budget	Final outturn	Expected outturn	Provision
Main Supply Estimates	104·5	104·5	108·3	116·0
x Supplementaries and net underspending	0·9	1·0	2·~~2~~ stet	
Total Supply expenditure	**105·3**	**105·5**	**110·5**	
Public expenditure element	79·5	79·6	~~84·8~~ 85·0	

FSBR

BUDGET CONFIDENTIAL

FROM: J. ANSON
1st March, 1989.

CHANCELLOR

c.c. PS/CST
PS/FST
PS/PMG
PS/EST
Sir P. Middleton
Sir T. Burns
Mr. Scholar
Mr. Culpin
Mr. Riley
Mr. Sedgwick
Mrs. Lomax
Mrs. R. J. Butler
Mr. McIntyre
Mr. S. Davies
Miss Simpson

Cl
OK? I've marked a few comments. AA

OK - one or two of mine, too.

Marked on text

1989 FSBR: CHAPTER 5

There are two small changes which I think we should make in the draft submitted to you today by Mrs. Butler:

(i) Delete the last sentence of paragraph 5.01. This is no longer true of the detailed plans. (It is still true of the overall total, but that is already made clear in the first line of paragraph 5.02.)

(ii) The first sentence of paragraph 5.04 should include figures for the public expenditure cost, both next year and in a full year. You have already asked for these to be included in a footnote to Table 1.1, but they ought to appear here also.

JA.

J. ANSON

COPY NO 23 OF 24

FROM: A C S ALLAN
DATE: 2 March 1989

may see pps
pr m

MR MACPHERSON

cc PS/Chief Secretary
PS/Financial Secretary
PS/Paymaster General
PS/Economic Secretary
Sir P Middleton
Sir T Burns
Mr Anson
Mr Scholar
Mr Culpin
Mr Riley
Mr Gilhooly
Mr Matthews
Miss Simpson
Mrs Chaplin
Mr Tyrie
Mr Call

Sir A Battishill IR
Mr Calder IR

Mr Unwin C&E
Mr P R H Allen C&E

FSBR CHAPTER 4

The Chancellor was grateful for your minute of 1 March. He had the following comments on your covering note and on the redraft of chapter 4.

(i) He does not understand why we cannot publish a "mature" yield from the life assurance package: surely the detailed work done on the costings provides a reliable basis? He would be grateful for further advice from FP and the Revenue on this.

(ii) He was content with your redraft of the second age allowance indent in paragraph 4.02.

(iii) Throughout the draft, you will need to take on board any changes that maybe made to the final package.

(iv) He was content with your neat solution of including the pensioners earnings rule as a National Insurance measure.

(v) He would prefer the final sentence of paragraph 4.31, on VAT on non-domestic construction, to be joined together so that it reads "VAT will also be applied from 1 April 1989 to protective boots and helmets supplied to employers, and to news services; and from 1 July 1990 it will be applied to fuel and power supplied to businesses, and to water and sewerage services supplied to industry.

(vi) The first two sentences of paragraph 4.37, on NICs, should be redrafted to read "From 2 October, the structure of employees' National Insurance contributions will be reformed. Employees will pay Class 1 contributions equal to 2 per cent of earnings up to the lower earnings limit....."

(vii) He was content with the Financial Secretary's redraft of paragraph 4.35, on Keith, subject to two small changes: amend the end of the first indent to read "...and provide the taxpayer with greater safeguards"; and amend the end of the third indent to read "....greater protection for the taxpayer".

(viii) Amend the manuscript addition to paragraph 9 of the annex to read "Tax yield of these measures will eventually be of the order of £100 million...."

ACSA

A C S ALLAN

BUDGET SECRET
BUDGET LIST ONLY
NOT TO BE COPIED

COPY NO: 1 OF 30 COPIES

FROM: COLIN MOWL
DATE: 1 March 1989

CHANCELLOR

cc Chief Secretary
Financial Secretary
Paymaster General
Economic Secretary
Sir P Middleton
Sir T Burns
Mr Anson
Mr Wicks
Mr Scholar
Mr Sedgwick
Mr Riley
Mr Culpin
Mrs Lomax
Mr S J Davies
Mr Hibberd
Mrs R Butler
Mr Pickford
Mr Gieve
Mr Patterson
Mrs Wright
Mrs Todd
Miss Simpson
Mrs Chaplin
Mr Tyrie
Mr Call

Mr Calder - IR
Mr Vernon - C&E

Cl
A few small comments
AA

A few comments, [illegible]

FSBR CHAPTER 6

I attach a first proof of chapter 6. It incorporates all the comments you made on the draft I circulated last week. None of the figures have changed - we will take on board revisions to the PSDR components next week.

2. In addition to any further comments you might have on the chapter there are two outstanding issues, debt and chart 6.4.

<u>Debt</u>

3. You suggested that we should say in paragraph 6.04 that the stock of net public sector debt at the end of 1988-89 is the lowest figure for x years. The problem is that this series only starts in 1975. But we are fairly certain that were the series available for earlier years the end-1988-89 figure would be the

lowest (relative to GDP) for some considerable time. What we propose therefore is that the remark should be couched in terms of "the stock of government debt", without making it clear which particular definition of debt is being referred to. We would base the remark on the figures for the National Debt which is the only available long series. (As far as we know net general government debt figures go back no further than 1972, but we are still checking.)

(seems OK?)

4. National Debt is, as you know, a gross central government measure of debt. The historical figures are attached. We have not yet worked out an end-1988-89 figure but we are fairly confident that it will be the lowest, relative to GDP, since before the First World War. I would advise against inclusion of an end-1988-89 figure for National Debt in the FSBR because it would detract from net public sector debt which we have said (eg. in the EPR in 1982) is the most appropriate measure of debt, mainly because it is the closest stock equivalent to the PSBR/PSDR. We are proposing however to include a National Debt estimate in the Budget brief.

Chart 6.4

5. You asked us to re-instate last year's chart 6.2 on the structure of receipts and expenditure. It will be chart 6.4 this year.

6. The chart is a graphical representation of table 1.2. There are therefore some slight changes to the chart reflecting this year's changes to the table. North Sea revenues are not shown separately - PRT and royalties are included with corporation tax - and the definitions of income tax and capital taxes are different. The former is now on a receipts not an accruals basis and the latter omits corporation tax on gains (now included in a wider measure of CT).

7. We are also offering you an alternative version of the chart which disaggregates expenditure taxes into VAT, whose share has risen sharply since 1978-79, and other expenditure taxes (largely the excise duties) whose share has fallen.

(Do we want to highlight this in year excise duties frozen?)

BUDGET SECRET
BUDGET LIST ONLY
NOT TO BE COPIED

8. You might also consider whether to let the chart speak for itself, as in previous years, or whether to draw attention in the text to its main features, namely,

- a fall in the share of income tax;
- a rise in the share of corporation tax (including certain oil taxes);
- a rise in the share of social security expenditure;
- a fall in the share of other departments (mainly due to DOE housing);

and, if the alternative version is used, a rising share of VAT and falling share of excise duties.

(You might note that our computer graphics package cannot handle more than eight categories of receipts or expenditure.)

<u>Conclusion</u>

9. We should be grateful for any further comments on the chapter, and your views on the proposed treatment of debt (paragraph 6.04) and presentation of chart 6.4 **<u>by lunch-time on Thursday</u>** (2 March) so that we can give the printers a revised version on Friday.

Colin Mowl

COLIN MOWL

BUDGET SECRET
BUDGET LIST ONLY
NOT TO BE COPIED

National debt and Net public sector debt

	NATIONAL DEBT		NET PUBLIC SECTOR DEBT	
	£billion	per cent of GDP(1)	£billion	per cent of GDP(1)
1855	0.8	105.0		
1860	0.8	98.7		
1865	0.8	81.4		
1870	0.8	71.5		
1875	0.8	59.0		
1880	0.8	58.0		
1885	0.7	57.2		
1890	0.7	47.4		
1895	0.7	42.6		
1900	0.6	32.3		
1905	0.8	36.7		
1910	0.7	31.9		
1911	0.7	29.6		
1912	0.7	28.4		
1913	0.7	26.3		
1914	0.7	25.5		
1915	1.1	35.3		
1916	2.1	59.7		
1917	4.0	88.4		
1918	5.9	112.0		
1919	7.4	133.1		
1920	7.8	130.9		
1921	7.6	147.5		
1922	7.7	167.2		
1923	7.7	176.6		
1924	7.6	172.9		
1925	7.6	163.6		
1926	7.6	172.0		
1927	7.6	163.8		
1928	7.5	161.6		
1929	7.5	158.7		
1930	7.5	159.4		
1931	7.4	170.1		
1932	7.4	173.9		
1933	7.6	179.5		
1934	7.8	173.3		
1935	7.8	165.2		
1936	7.8	158.9		
1937	7.8	147.4		
1938	8.0	144.0		
1939	8.2	138.0		
1940	8.9	118.7		
1941	11.4	129.1		
1942	14.1	146.7		
1943	16.9	165.1		
1944	19.6	190.8		
1945	22.4	227.8		
1946	24.7	247.7		
1947	25.6	240.6		
1948	25.6	218.5		
1949	25.2	203.2		
1950	25.8	199.5		
1951	25.9	179.8		
1952	25.9	165.6		
1953	26.1	154.7		
1954	26.6	149.7		
1955	26.9	141.0		
1956	27.0	130.9		
1957	27.0	123.6		
1958	27.2	119.7		
1959	27.4	113.8		
1960	27.7	107.1		
1961	28.3	103.0		
1962	28.7	99.4		
1963	29.8	98.7		
1964	30.2	91.4		
1965	30.4	85.0		
1966	31.3	82.0		
1967	32.0	79.4		
1968	34.2	79.3		
1969	34.0	72.8		
1970	33.1	65.2		
1971	33.4	59.3		
1972	35.8	57.0		
1973	37.2	51.5		
1974	40.5	50.3		
1975	46.4	46.5	59.5	59.6
1976	56.6	47.2	71.8	60.0
1977	66.9	47.6	81.3	57.9
1978	79.2	48.8	87.9	54.2
1979	86.9	46.1	95.3	50.6
1980	95.6	42.7	102.1	45.6
1981	113.3	45.6	116.5	46.9
1982	118.6	43.5	127.2	46.7
1983	128.2	43.3	135.0	45.5
1984	143.1	45.0	147.3	46.2
1985	158.3	45.7	160.7	46.4
1986	171.6	46.0	166.8	44.8
1987	185.7	45.9	171.1	42.3
1988	197.3	44.3	171.3	38.6
1989			[157]	[31.5]

(1) GDP centered on 31 March for 1959 to 1988, and calender year GDP used prior to 1959.

(2) Sources
GDP:- 1946 to 1988 CSO series EBAA
GDP:- 1855 to 1945 Feinstein
National Debt and Net Public Sector Debt:- Bank of England Quarterly Bulletin

6 The public sector's finances

The scope of this chapter

6.01. This chapter brings together revenue and spending and provides an analysis and forecast of the public sector's overall financial position in 1989–90, together with some explanation of the main differences between estimated outturn in 1988–89 and last year's forecast.

Debt repayment

6.02. The latest estimate is for a public sector debt repayment (PSDR) of £14 billion in 1988–89, equivalent to 3 per cent of GDP, or £7 billion excluding privatisation proceeds. Even this last figure represents a larger net repayment as a proportion of GDP than in any year since the beginning of the 1950s—the earliest date for which comparable figures are available. Both the public sector financial balance and the general government financial balance are also estimated to be in substantial surplus in 1988–89.

6.03. The forecast is for a further substantial PSDR of around £12 billion about in 1989–90. Excluding privatisation proceeds the PSDR is forecast to be the same in 1989–90 as in 1988–89.

Table 6.1 Public sector debt repayment

	£ billion and as per cent of GDP			
	1987–88	1988–89		1989–90
	Outturn	1988 Budget	Latest estimate	Forecast
Public sector debt repayment				
£ billion	3·5	3·2	14·0	12·1
as per cent of GDP	¾	¾	3	2¼
PSDR excluding privatisation proceeds				
£ billion	−1·6	−1·8	7·0	7·1
General government borrowing requirement as per cent of GDP	−½	−½	1½	1½

6.04. The stock of net public sector debt has fallen from over 50 per cent of money GDP in 1979 to 38½ per cent (£171 billion) at the end of 1987–88. It is forecast to be about £[157] billion, or [31½] per cent of GDP, at the end of 1988–89. Relative to GDP the stock of government debt is now lower than at any point since before the First World War. There should be a further large fall in net public sector debt in 1989–90, in both nominal terms and as a percentage of GDP.

OK?
OK Thanks:

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

Changes since last Budget

6.05. The PSDR in 1988–89 is now estimated to be nearly £11 billion higher than forecast in last year's Budget. As table 6.2 shows the higher net repayment comes roughly equally from higher receipts and lower expenditure, including £2 billion additional privatisation proceeds (see table 1.2 for a detailed comparison of the components). Much of the extra receipts reflects the higher than forecast growth of money GDP. Higher growth has also contributed to the lower than forecast expenditure, primarily through lower spending on social security and improved finances of public corporations.

Table 6.2 Changes to receipts, expenditure and debt repayment since 1988 Budget[1]

	£ billion 1987–88	1988–89
Receipts		
Taxes, royalties and national insurance contributions	+0·8	+4·8
Other receipts	−0·7	+1·1
Total	**+0·2**	**+5·9**
Expenditure		
Privatisation proceeds	−0·1	−2·0
Other general government	+0·2	−2·4
Public corporations' market and overseas finance	−0·4	−0·6
Total	**−0·3**	**−5·0**
PSDR	**+0·5**	**+10·8**

[1] *+ higher receipts, higher expenditure, or higher debt repayment;*
− lower receipts or lower expenditure.

6.06. The main contributors to the higher than expected receipts are income tax (£1½ billion), national insurance contributions (£1 billion), VAT (£1¼ billion) and interest receipts (£1 billion). The first two largely reflect higher total wages and salaries. Higher VAT receipts are the result of faster growth of consumer spending in total and a change in its composition towards those goods and services which are subject to VAT.

6.07. Corporation tax receipts again rose strongly in 1988–89 but not by as much as forecast. Within the total, advance corporation tax (ACT) receipts were higher than forecast, reflecting high dividend payments in 1988, but other corporation tax receipts rose much less than expected. The latter is likely to be mainly the result of lower profits and higher investment in 1987 than shown by the recorded figures available at the time of the last Budget.

PS/ Chase | no reply to query is this true?

6.08. Privatisation proceeds were £2 billion higher than projected at the time of the last Budget. Expenditure excluding privatisation proceeds was lower than forecast, largely as a result of lower social security expenditure and higher local authority capital receipts.

6.09. The public sector's finances can be analysed in a number of different ways: by type or activity, by sector and by economic category. The rest of this chapter sets out these three analyses in detail.

BUDGET SECRET
BUDGET LIST ONLY
NOT TO BE COPIED

Public sector's finances: analysis by type or activity

6.10. Table 1.2 analyses the public sector's finances by type or activity. The main receipts of general government (ie central plus local government) are grouped according to the kind of activity which gives rise to them, while spending is shown by department, as in Chapter 5 and in the public expenditure White Paper.

Receipts **6.11**. General government receipts are estimated to have risen by 9½ to 10 per cent in 1988–89, just below the growth of money GDP. They are forecast to rise by 6½ to 7 per cent in 1989–90, a little less than the forecast growth of money GDP.

Within general government receipts,   Fell sharply in 1988-89, as forecast. They   a further

6.12. North Sea revenues are forecast to fall by 15 per cent in 1989–90, mainly the delayed effect on corporation tax of falling profits in earlier years. Oil production is expected to be lower in 1989 than in 1988, due mainly to the continued effect of the Piper Alpha disaster and accidents in the Fulmar and Brent fields. The forecast assumes that North Sea oil prices will remain close to recent levels. PRT receipts are forecast to be the same in 1989–90 as in 1988–89 despite the projected fall in production because there were repayments of advance PRT in 1988–89 and none are forecast for 1989–90.

as a result of

Table 6.3 North Sea revenues

	£ billion			
	1987–88	1988–89		1989–90
	Outturn	1988 Budget	Latest estimate	Forecast
North Sea corporation tax[1]	1·4	1·5	1·3	0·8
Petroleum revenue tax[2]	2·3	1·2	1·3	1·3
Oil royalties	1·0	0·6	0·6	0·6
Total North Sea revenues	**4·7**	**3·3**	**3·2**	**2·7**
[1]*before ACT set off of:*	*0·7*	*0·8*	*0·8*	*0·5*

[2]*includes advance petroleum revenue tax*

6.13. Excluding North Sea revenues general government receipts rose by over 10½ per cent in 1988–89 and are forecast to rise by about 7 per cent in 1989–90. Within the overall increase forecast for 1989–90 there is:

an 8 per cent increase in income tax receipts;

an 18 per cent increase in non-oil corporation tax, with ACT growing more slowly than the rest;

an 8 per cent increase in VAT receipts, a little less than the increase in consumers' expenditure, reflecting relatively slow growth of spending subject to VAT;

little change in receipts from the excise duties on petrol, tobacco and alcohol;

an 8 per cent increase in local authorities' net receipts of rates (and community charge in Scotland);

a 5½ per cent increase in national insurance contributions, after allowing for the reforms to employees' contributions announced in the Budget.

BUDGET SECRET
BUDGET LIST ONLY
NOT TO BE COPIED

0230

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

BUDGET

Taxes as a share of GDP

6.14. Table 6.4 shows total taxes and national insurance contributions (NICs) as a percentage of GDP. Both the total and non-oil percentages are estimated to have fallen in 1988–89, by about half a percentage point in each case, compared with a forecast of no change in last year's Budget. Given the payments lags in the tax system a fall in the percentage is likely when there is a pick-up in the growth of money GDP. Some taxes, such as mainstream corporation tax, are paid some time after the period for which the liability is incurred. For over 20 per cent of total tax receipts the payments lags are one year or longer; receipts of these taxes are therefore unaffected by changes in GDP in the same year. With other taxes, stamp duty for example, there is a variable relationship between changes in the tax base and changes in money GDP.

6.15. The forecast is for non-oil taxes and NICs to be the same as a percentage of ~~money~~ non-oil GDP in 1989–90 as in 1988–89. In other words, the changes in the Budget ~~nearly~~ merely offset real fiscal drag—the tendency for average tax rates to rise in a progressive tax system indexed to price changes. With the projected fall in North Sea revenues in 1989–90, total taxes and NICs are forecast to fall slightly as a percentage of GDP.

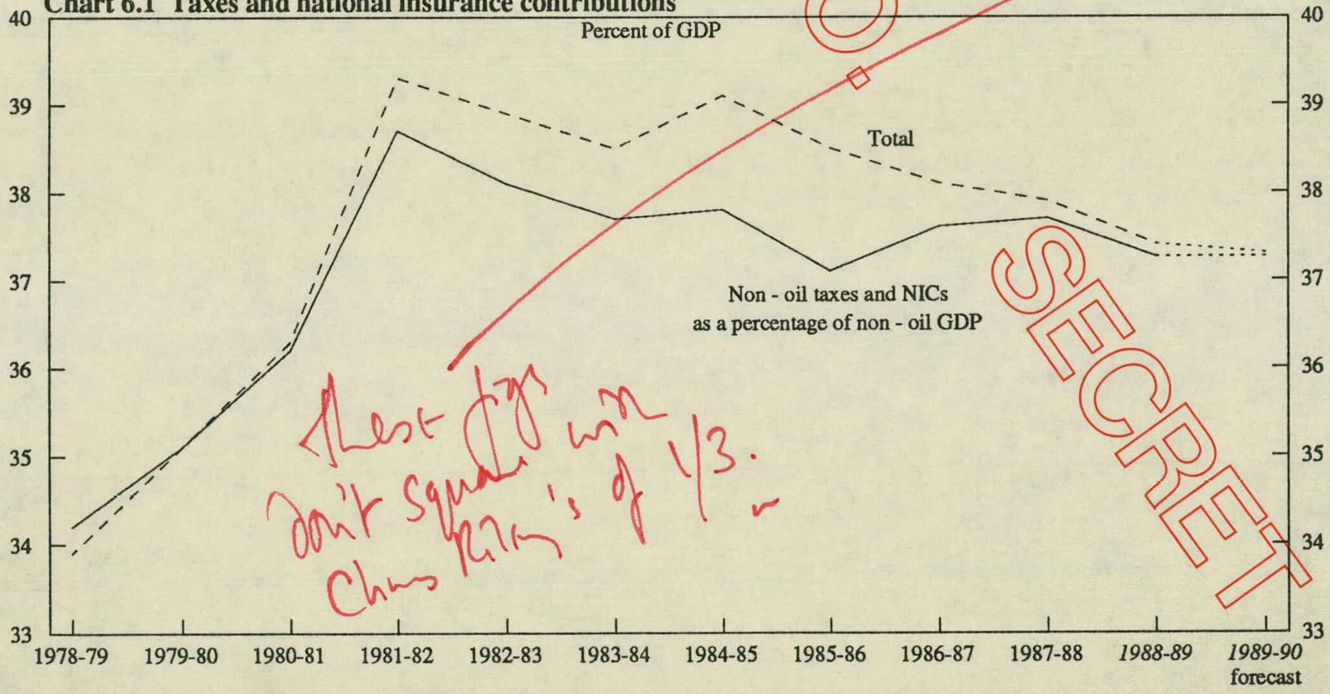
SECRET

Table 6.4 Taxes and national insurance contributions as a percentage of GDP

	1983–84	1984–85	1985–86	1986–87	1987–88	1988–89 Latest estimate	1989–90 Forecast
Total taxes and NICs as a share of total GDP	38·5	39·1	38·5	38·1	37·9	37·4	37·2
Non-oil taxes and NICs as a share of non-oil GDP	37·7	37·8	37·1	37·6	37·7	37·3	37·3

B.L.O.

Chart 6.1 Taxes and national insurance contributions



These figs don't square with Chris Riley's of 1/3.

SECRET

BUDGET SECRET
BUDGET LIST ONLY

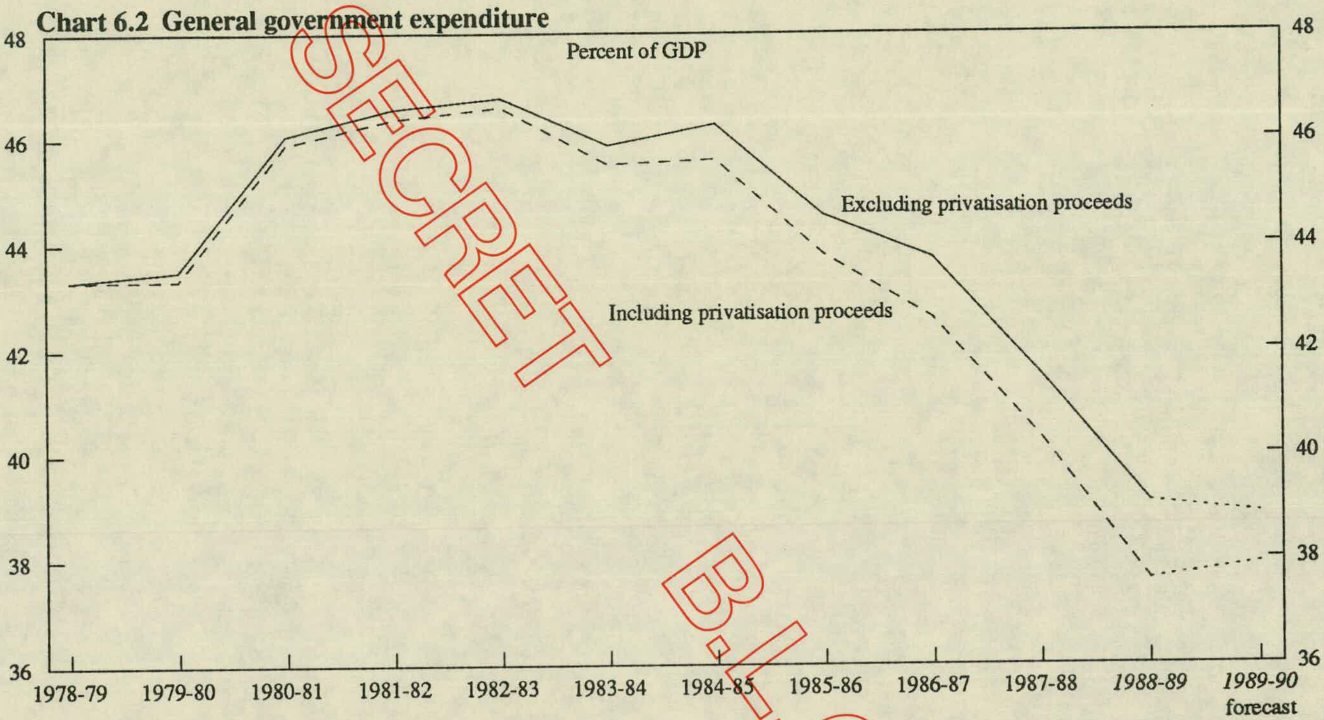
NOT TO BE COPIED

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

Expenditure **6.16**. General government expenditure (GGE) excluding privatisation proceeds is now estimated to have increased by under 5 per cent in 1988–89, and is forecast to rise by nearly 7 per cent in 1989–90, below the growth of money GDP in both years. The ratio of GGE excluding privatisation proceeds to money GDP is therefore expected to fall in both years, as illustrated in chart 6.2.

Chart 6.2 General government expenditure



6.17. Within GGE, gross debt interest payments rose in cash terms in 1988–89 partly because of higher interest rates and inflation (which raises the cost of servicing indexed debt). Net debt repayment reduces interest payments, other things being equal, but not immediately; and because of the rise in the foreign exchange reserves and other short-term assets in 1987–88 and early 1988–89 some of the effect has come through initially as higher interest receipts. Interest and dividend receipts rose by £½ billion in 1988–89, despite a fall in the dividend element following the sale of the Government's remaining shareholding in BP.

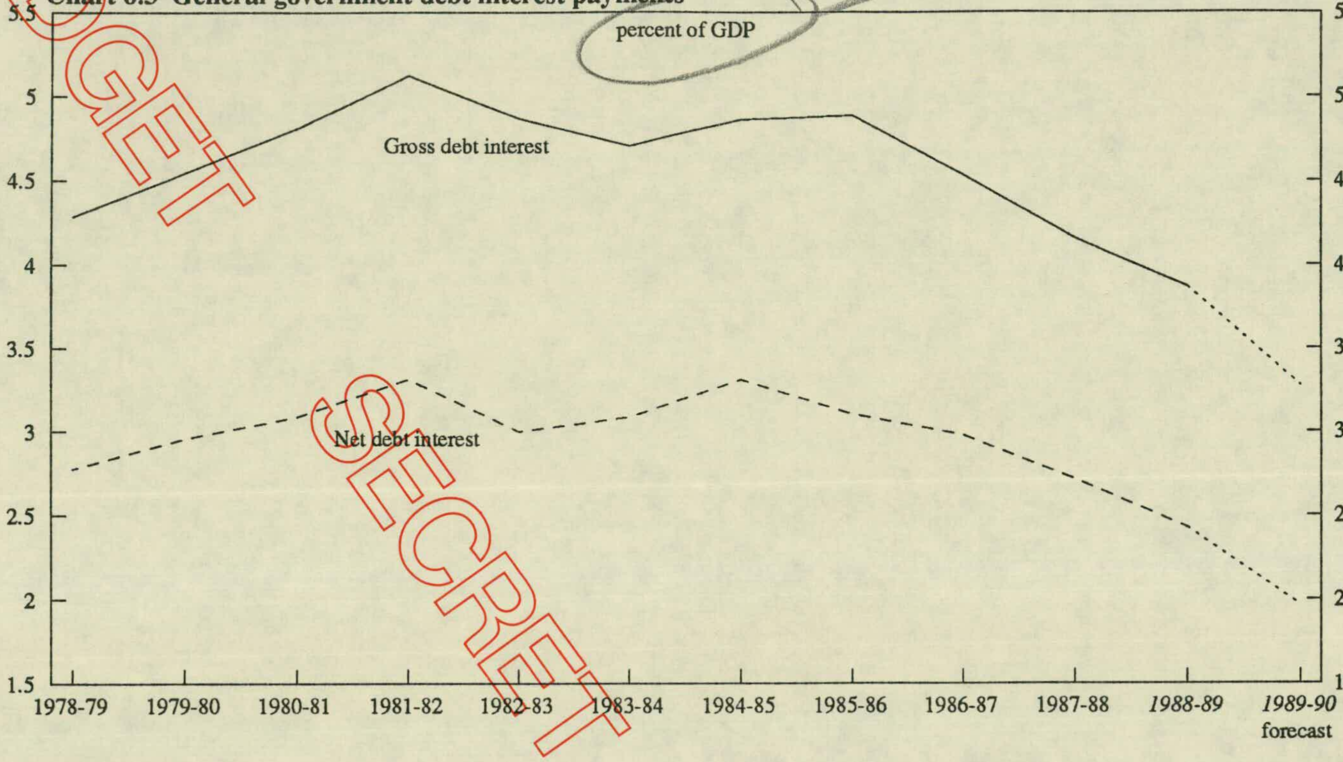
6.18. Debt interest payments are forecast to fall substantially in 1989–90, against a background of no change in interest and dividend receipts.

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

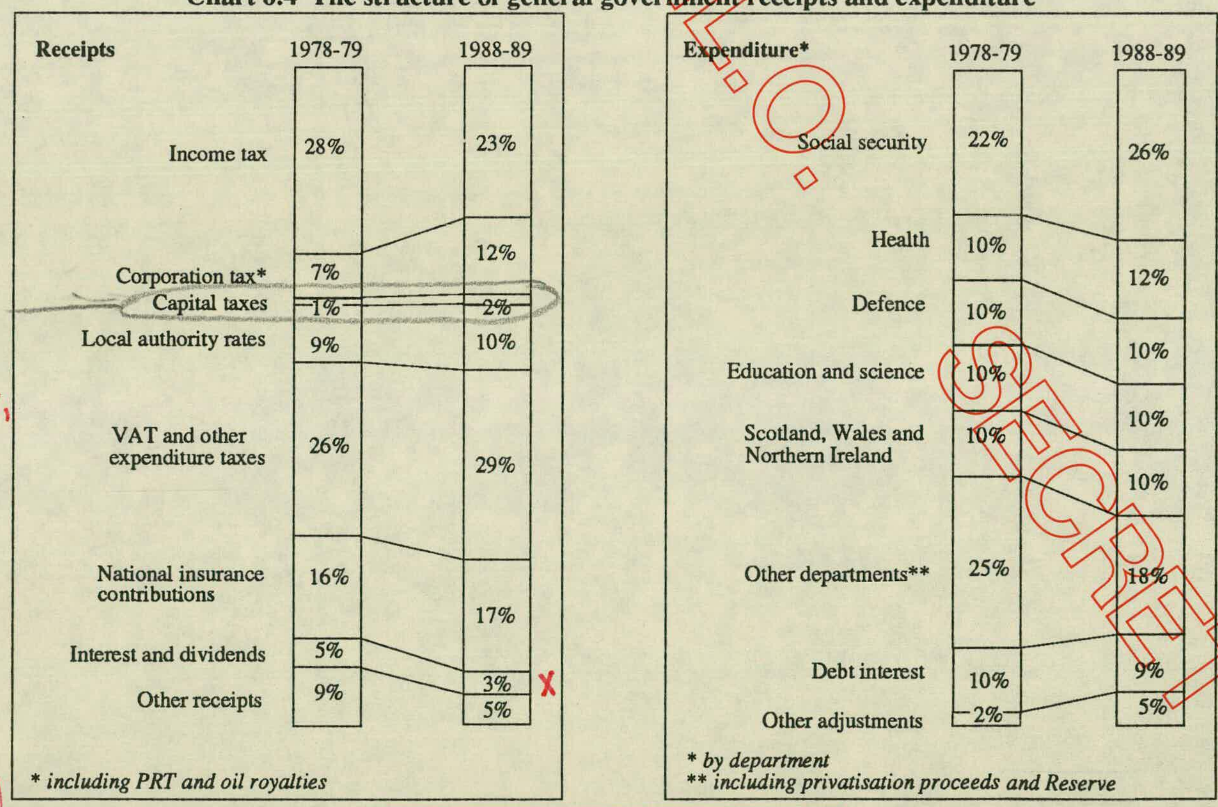
Much better

Chart 6.3 General government debt interest payments



6.19. Chart 6.4 shows the changes in the structure of general government receipts and expenditure which have taken place since 1978–79.

Chart 6.4 The structure of general government receipts and expenditure



clumsy setting

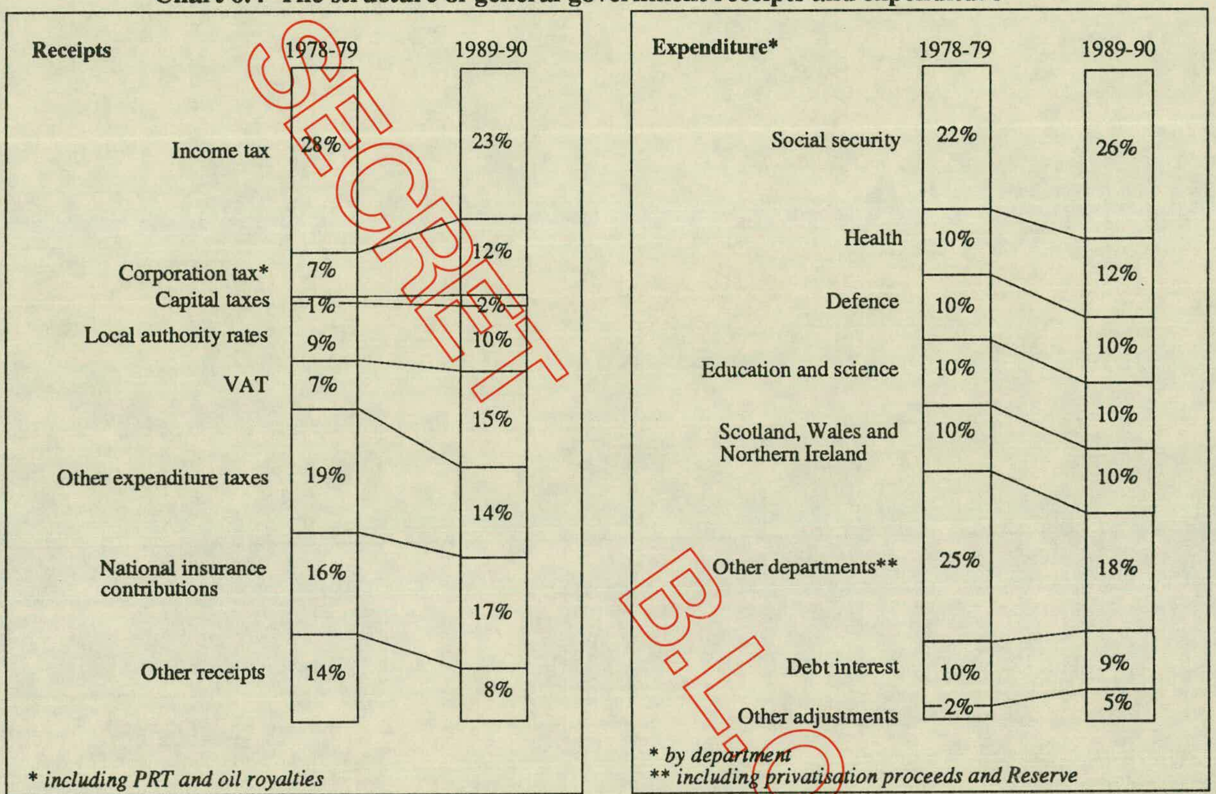
Better to have band slightly; figures tells story. (So long as [illegible] handle [illegible] will do)

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

Alternative version of chart 6.2 with expenditure taxes disaggregated into VAT and other.

Chart 6.4 The structure of general government receipts and expenditure



No thanks. Use first version, which makes it easier to see overall income tax/expenditure tax switch

Public sector's finances: analysis by sector

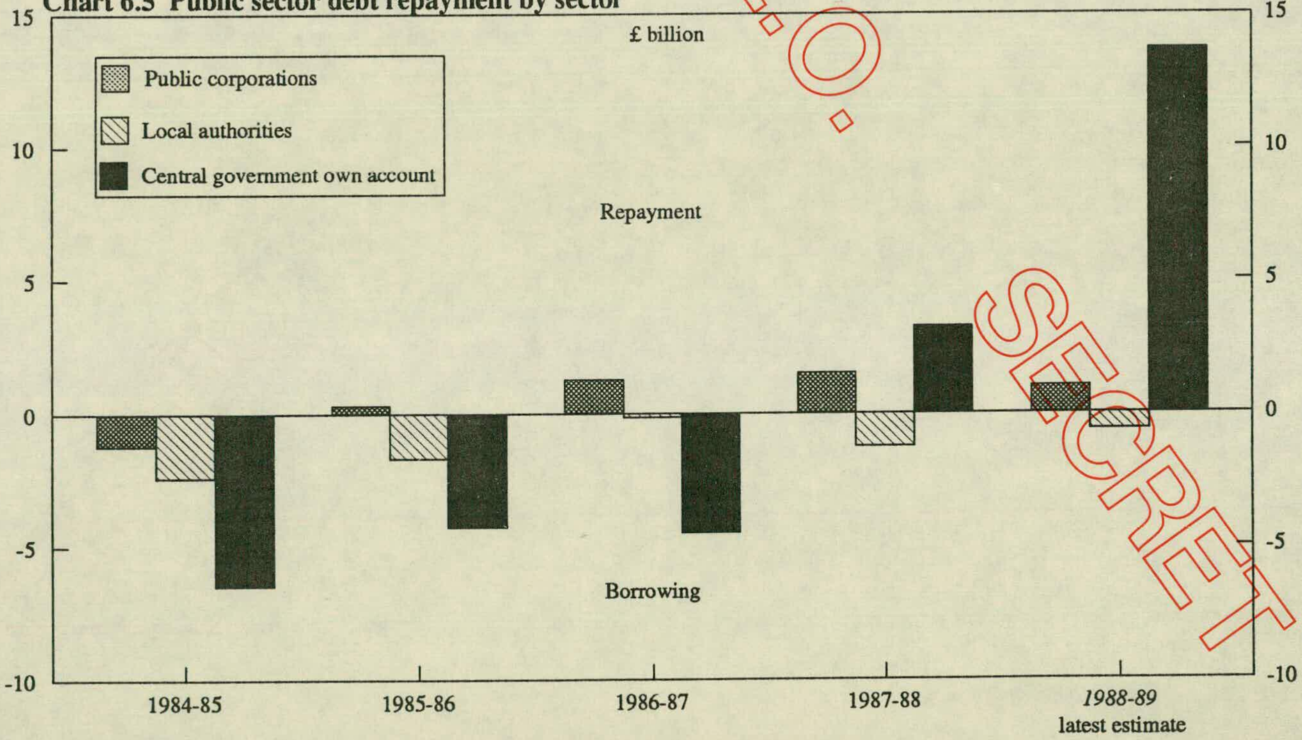
6.20. Table 6.5 shows net ~~borrowing~~ debt repayment in 1987–88 and 1988–89 by central government, local authorities and public corporations.

Table 6.5 Public sector debt repayment

	£ billion			
	1987–88 Outturn		1988–89 Latest estimate	
1 Central government debt repayment on own account	**3·2**		**13·7**	
2 Local authority debt repayment	**−1·2**		**−0·6**	
3 of which to: central government		−4·1		−4·5
4 market and overseas		2·9		3·9
5 Public corporations' debt repayment	**1·5**		**1·0**	
6 of which to: central government		0·0		−0·8
7 market and overseas		1·5		1·7
8 Public sector debt repayment	**3·5**		**14·0**	
Central government debt repayment (lines 1+3+6)		−0·9		8·5

6.21. The PSDR in the first ten months of 1988–89 was £15·5 billion, substantially higher than in the same period of 1987–88, both including and excluding privatisation proceeds. The greater part of the increase was on central government own account. Taking into account both further privatisation proceeds of about £1 billion due in March and the well established pattern of high borrowing in March, the forecast for 1988–89 as a whole is a public sector net debt repayment of £14 billion.

Chart 6.5 Public sector debt repayment by sector



6.22. Tables 6.6 to 6.8 show estimated outturns and forecasts of receipts and expenditure in 1988–89 and 1989–90 for each of the three sectors. Expenditure in 1989–90 does not include an allocation of the Reserve, although the forecast of the PSDR assumes that the Reserve is fully spent.

Central government 6.23. Central government expenditure in table 6.6 includes grants and subsidies to local authorities and public corporations (including nationalised industries), which are included in the receipts of those sectors, shown in Table 6.7 and 6.8. The forecast large rise in 1989–90 in net lending etc is mainly the result of a lower level of privatisation proceeds.

Table 6.6 Central government transactions

	£ billion 1987–88 Outturn	1988–89 Latest estimate	1989–90 Forecast[1]
Receipts			
Taxes and royalties	115·8	125·9	135·3
National insurance and other contributions	29·0	32·8	34·6
Other	10·4	11·4	10·8
Total receipts	**155·1**	**170·1**	**180·6**
Expenditure			
Current expenditure on goods and services	52·5	56·8	61·5
Current grants and subsidies	80·5	80·0	86·2
Interest	17·2	17·6	16·2
Net lending[2], capital expenditure, and cash expenditure on company securities	1·6	2·0	4·8
Total expenditure	**151·8**	**156·4**	**168·7**
Consolidated Fund revenues	123·0	135·5	141·2

whole row small italics

[2] *Excluding lending to local authorities and public corporations.*
[1] *Excluding any allocation from the Reserve.*

, in Scotland,
(and (community charge income

Local authorities 6.24. Local authority receipts consist primarily of rate income plus grants from central government. The forecast increase in rate income (net of ~~rate~~ rebates) between 1988–89 and 1989–90 takes account of available information about rate decisions by local authorities, ~~and~~ additions to rateable value, (and) ~~The forecast of receipts is consistent with~~ the announced levels of community charge in Scotland. The forecast of expenditure in 1989–90 is lower than it would otherwise have been because of the transfer of polytechnics from the local authority to the private sector.

and community charge

6.25. From information available about the first ten months it looks as if the local authority borrowing requirement will turn out to be rather lower in 1988–89 than in 1987–88, partly due to lower net capital spending as a result of rising capital receipts.

Table 6.7 Local authority transactions

	£ billion		
	1987–88 Outturn	1988–89 Latest estimate	1989–90 Forecast[1]
Receipts			
Rates and community charge[2]	17·0	18·9	20·4
Rate and revenue support grant	12·5	12·7	13·0
Other grants from central government	12·0	12·2	12·9
Other	5·4	5·9	7·0
Total receipts	**46·9**	**49·7**	**53·3**
Expenditure			
Current expenditure on goods and services	34·6	36·4	37·0
Current grants and subsidies	5·5	6·0	6·8
Interest	4·4	4·7	4·8
Net lending and capital expenditure	3·6	3·3	2·5
Total expenditure	**48·1**	**50·4**	**51·0**[2]
2 1 Net of rate rebates.	*1·9*	*1·6*	*1·6*

1 ~~2~~ Excluding any allocation from the Reserve.

Public corporations 6.26. Table 6.8 shows public corporations' transactions. The public corporations' receipts include subsidies and capital grants from central and local government. Changes in public corporations' income and expenditure from one year to another are affected by privatisations which involve re-classifying privatised industries from the public to the private sector in the national accounts. For example the 12 per cent increase in gross trading surplus in 1988–89 would have been larger had British Steel not been excluded, following its privatisation.

Table 6.8 Public corporations' transactions

	£ billion		
	1987–88 Outturn	1988–89 Latest estimate	1989–90 Forecast[1]
Receipts			
Gross trading surplus (including subsidies)	6·8	7·6	8·1
Other	2·4	2·0	2·6
Total receipts	**9·2**	**9·6**	**10·7**
Expenditure			
Interest, dividends and taxes on income	3·1	3·3	3·6
Net lending and capital expenditure	4·5	5·4	5·8
Total expenditure	**7·6**	**8·6**	**9·4** X
Public corporations' contribution to planning total:			
nationalised industries' external finance	*0·3*	*0·4*	*0·0*
other public corporations	*0·5*	*0·6*	*0·9*

[1] Excluding any allocation from the Reserve

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

Public sector's finances: analysis by economic category

6.27. The full analysis of receipts and expenditure by economic category is shown in Table 6.9, with a breakdown between central government, local authorities and public corporations. This analysis, which distinguishes between current and capital transactions (and within the latter between physical and financial investment), shows the derivation of the public sector financial surplus. The financial surplus, unlike the PSDR, is not wholly a measure of cash transactions because certain items above line 24 in Table 6.9, for example some taxes included in lines 1 and 2, are measured on an accruals basis. An accruals adjustment is accordingly made in line 28.

6.28. The unallocated Reserve is assumed to be on current spending items or physical capital formation ie in transactions that fall above the financial surplus line. In practice allocations from the Reserve can affect financial transactions (lines 25 to 29).

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

Table 6.9 Public sector transactions by sub-sector and economic category

£ billion

1988–89 Latest estimate

	Line[1]	General government: Central government	General government: Local authorities	General government: Total	Public corporations	Public sector
Current and capital receipts						
Taxes on income, and oil royalties	1	62·8	—	62·8	−0·2	62·6
Taxes on expenditure[2]	2	57·9	18·9	76·7	—	76·7
Taxes on capital	3	5·2	—	5·2	—	5·2
National insurance and other contributions	4	32·8	—	32·8	—	32·8
Gross trading surplus	5	−0·5	0·7	0·2	7·6	7·9
Rent and miscellaneous current transfers	6	0·4	2·8	3·2	0·5	3·8
Interest and dividends from private sector and abroad	7	3·4	1·2	4·6	0·7	5·2
Interest and dividends within public sector	8	6·0	−4·0	2·0	−2·0	—
Imputed charge for non-trading capital consumption	9	1·3	1·6	2·9	—	2·9
Capital transfers from private sector	10	—	—	—	0·2	0·2
Total receipts	11	**169·4**	**21·2**	**190·5**	**6·7**	**197·3**
Current and capital expenditure						
Current expenditure on goods and services	12	56·8	36·4	93·2	—	93·2
Subsidies	13	4·0	1·0	4·9	—	4·9
Current grants to personal sector	14	49·2	5·0	54·2	—	54·2
Current grants paid abroad	15	2·9	—	2·9	—	2·9
Current grants within public sector	16	24·0	−23·9	—	—	—
Debt interest	17	17·6	0·6	18·2	0·6	18·8
Gross domestic fixed capital formation	18	4·0	2·9	6·9	5·0	11·9
Increase in stocks	19	−0·3	—	−0·3	0·3	0·1
Capital grants to private sector	20	3·1	0·6	3·6	0·1	3·7
Capital grants within public sector	21	1·8	−1·0	0·8	−0·8	—
Total expenditure	22	**163·0**	**21·5**	**184·5**	**5·2**	**189·8**
Unallocated Reserve	23	—	—	—	—	—
Financial surplus	24	**6·3**	**−0·4**	**6·0**	**1·5**	**7·5**
Financial transactions						
Net lending to private sector and abroad	25	0·5	−0·3	0·3	—	0·3
Cash expenditure on company securities (including privatisation proceeds)	26	−7·1	0·1	−7·0	—	−7·1
Transactions concerning certain public sector pension schemes	27	−0·7	—	−0·7	—	−0·7
Accruals adjustments	28	−0·1	−0·2	−0·4	—	−0·3
Miscellaneous financial transactions	29	0·1	0·7	1·3	0·6	1·4
Debt repayment	30	**13·7**	**−0·6**	**13·1**	**1·0**	**14·0**

[1] *Financial surplus (line 24) = receipts (line 11) − expenditure (line 22) − Reserve (line 23). Debt repayment (line 30) = financial surplus (line 24) − financial transactions (lines 25 to 29).*

[2] ~~and~~ including community charge in Scotland.

BUDGET SECRET
BUDGET LIST ONLY

NOT TO BE COPIED

£ billion

1989–90 Forecast

Line[1]	General government: Central government	General government: Local authorities	General government: Total	Public corporations	Public sector	
						Current and capital receipts
1	69·2	—	69·2	−0·6	68·5	Taxes on income, and oil royalties
2	60·8	20·4	81·2	—	81·2	Taxes on expenditure[2]
3	5·3	—	5·3	—	5·3	Taxes on capital
4	34·6	—	34·6	—	34·6	National insurance and other contributions
5	−0·5	0·8	0·3	8·1	8·4	Gross trading surplus
6	0·3	3·0	3·3	0·7	4·0	Rent and miscellaneous current transfers
7	3·2	1·4	4·5	0·6	5·1	Interest and dividends from private sector and abroad
8	6·5	−4·2	2·3	−2·3	—	Interest and dividends within public sector
9	1·4	1·7	3·1	—	3·1	Imputed charge for non-trading capital consumption
10	—	—	—	0·2	0·2	Capital transfers from private sector
11	**180·8**	**23·0**	**203·8**	**6·7**	**210·5**	**Total receipts**
						Current and capital expenditure
12	61·5	37·0	98·5	—	98·5	Current expenditure on goods and services
13	4·4	0·9	5·3	—	5·4	Subsidies
14	52·9	5·8	58·8	—	58·8	Current grants to personal sector
15	4·0	—	4·0	—	4·0	Current grants paid abroad
16	24·8	−24·8	—	—	—	Current grants within public sector
17	16·2	0·4	16·6	0·5	17·1	Debt interest
18	5·0	1·9	6·9	5·6	12·5	Gross domestic fixed capital formation
19	−0·2	—	−0·1	0·2	−0·1	Increase in stocks
20	2·4	0·7	3·1	0·1	3·2	Capital grants to private sector
21	2·2	−1·1	1·1	−1·1	—	Capital grants within public sector
22	**173·3**	**21·0**	**194·3**	**5·2**	**199·5**	**Total expenditure**
23					3·5	Unallocated Reserve
24					**7·5**	**Financial surplus**
						Financial transactions
25	0·4	−0·2	0·2	—	0·2	Net lending to private sector and abroad
26	−5·0	—	−5·0	—	−5·0	Cash expenditure on company securities (including privatisation proceeds)
27	−0·3	—	−0·3	—	−0·3	Transactions concerning certain public sector pension schemes
28	−0·6	−0·2	−0·8	—	−0·8	Accruals adjustments
29	1·0	0·2	1·2	0·1	1·3	Miscellaneous financial transactions
30					**12·0**	**Debt repayment**